

EXHIBIT G

1

2 UNITED STATES BANKRUPTCY COURT

3 | SOUTHERN DISTRICT OF NEW YORK

4 Case No. 08-10595-smb

6 | In the Matter of:

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8 WELLMAN, INC.

9

10 Debtor.

11

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14 United States Bank

15 One Bowling Green

16 New York, New York

17

18 August 5 2008

19 12:10 PM

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21 | B E F O R E :

22 HON. STUART M. BERNSTEIN

23 U.S. BANKRUPTCY JUDGE

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2 HEARING re Closing Arguments on Motion on Valuation of
3 Collateral

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1 P R O C E E D I N G S

2 THE COURT: Please be seated. Okay, Wellman.

3 MR. SERINO: Good morning, Your Honor.

4 THE COURT: Good morning -- or afternoon.

5 MR. SERINO: Afternoon, I should say, yeah.

6 THE COURT: Well, you got caught behind a longer
7 proceeding than I thought it would go.

8 MR. SERINO: That's fine. May I proceed?

9 THE COURT: Sure.

10 MR. SERINO: Joe Serino for the debtors. Your Honor,
11 I'd like to begin by thanking the Court and the Court's staff
12 for making the courthouse so accommodating to all of us over
13 the last couple of days and for treating all of the
14 participants here with courtesy and professionalism.

15 THE COURT: Really? What did we do?

16 MR. SERINO: Let us leave our stuff here. Let us --

17 THE COURT: Okay. Oh.

18 MR. SERINO: -- make home, set up shop here. We
19 appreciate it.

20 THE COURT: Well, you'll get the bill.

21 MR. SERINO: I said at the opening, Your Honor, that
22 the parties agree on the standard here and the only problem was
23 they disagree on how it should be applied.

24 THE COURT: As I recall, Mr. Henes said it was a very
25 narrow dispute.

1 MR. SERINO: That's exactly right.

2 MR. HENES: I still think it is.

3 MR. SERINO: I'll tell you, though, after listening
4 to the opening statements of the first liens, I'm not sure that
5 that's really the problem. I think the first liens know how
6 Rash is to be applied. And I think the problem here is that
7 their counsel talked about the need to come up with a value for
8 a bare naked plan. And I think that's probably fine. I think
9 the problem is that the first lien's expert, Mr. Lerman, didn't
10 come up with a value for a bare naked plan.

11 THE COURT: What are the components of the valuations
12 that are so different that they lead to different results?
13 You're essentially 113 million dollars --

14 MR. SERINO: Yes.

15 THE COURT: -- apart. Why?

16 MR. SERINO: Well, I think the biggest component,
17 Your Honor, is that Mr. Lerman, even in his technology
18 disconnection scenario, he said on cross-examination, I took
19 out for intellectual property but I still assume that the PP&E
20 was sold as part of a going concern. I still did a going-
21 concern valuation. So what Mr. Lerman did is he heaped on top
22 of that PP&E the value that comes from working capital and all
23 the intangible assets and all the going-concern value that the
24 first do not have a lien over.

25 THE COURT: How did he do that?

1 MR. SERINO: Because he never stripped out for it.
2 He never isolated out for it. The only thing he isolated out
3 for was -- he took a business enterprise and the only thing he
4 took out for was the intellectual property.

5 THE COURT: Right.

6 MR. SERINO: He never took out for the other going-
7 concern attributes.

8 THE COURT: Well, what else was that besides working
9 capital which he subtracted?

10 MR. SERINO: All of the going-concerns, labor force,
11 the sales force, the customer force, the processes, the
12 systems. All of that.

13 THE COURT: But he assumed a delay. As I understood
14 his worst case scenario, which was, I think, the 139 million
15 dollar valuation --

16 MR. SERINO: Yeah. 138.6.

17 THE COURT: He said if a buyer in the industry went
18 to the PP&E store and bought this stuff, this is what the
19 expense would be to get it up and running in sixty days.

20 MR. SERINO: Mr. Lerman said that?

21 THE COURT: That's what I understood his testimony to
22 be.

23 MR. SERINO: I thought Mr. Lerman said is if a buyer
24 came to the table and had all the bundle of sticks and he had
25 all of the intangible assets --

1 THE COURT: Well, I'm talking about his last
2 scenario.

3 MR. SERINO: I thought it was the same thing for his
4 last scenario with the one exception is he tried to isolate out
5 the value of the intellectual property. I still think that
6 he -- he testified on cross-examination that but for that, I'm
7 assuming the plant was being sold as a going concern. I think
8 that's the fundamental problem here, Your Honor. When he
9 assumed it was being sold as a going-concern, he assigned to
10 the PP&E lots of value that's associated with a going concern.

11 THE COURT: What were the differences in his analysis
12 and Mr. Schmitt's analysis about the aggregate revenues for
13 instance that the companies would receive over the objection
14 period.

15 MR. SERINO: Your Honor, I don't remember off the top
16 of my hand the differences in the revenues but I do remember
17 the differences in the total business enterprise value, if
18 that's helpful. Mr. Schmitt came out at 273 million dollars --

19 THE COURT: Right.

20 MR. SERINO: -- through the DCF and the two market
21 approaches. Mr. Lerman was anywhere from 366 million to 400
22 million --

23 THE COURT: Well, let's take his middle approach
24 which is some technology but not all of it. So what did he
25 come out with there?

1 MR. SERINO: I think his -- I don't remember what his
2 business enterprise value was but I think his valuation of the
3 PP&E in that scenario, if that's what Your Honor wants --

4 THE COURT: Well, no. I'm asking about --

5 MR. SERINO: -- was 181.8 million.

6 THE COURT: Okay. And what --

7 MR. SERINO: But the problem there was he admittedly
8 incorporated certain patents, certain trademarks and certain
9 licenses that the firsts simply do not have a lien on.

10 THE COURT: Um-humm.

11 MR. SERINO: That was in his middle scenario. In his
12 last scenario, the technology disconnection scenario, he tried
13 to correct for that. But our point is he still didn't go far
14 enough. His counsel stood up in the opening and said you got a
15 value of bare naked plant. But he didn't value a bare naked
16 plant. He valued a plant that was sold as part of a going
17 concern. And he didn't strip out all those going-concern
18 elements of value.

19 THE COURT: But doesn't -- and I asked this at the
20 beginning. Doesn't the PP&E have more value simply because
21 it's a going-concern --

22 MR. SERINO: And I think you're right, Your Honor.

23 I --

24 THE COURT: -- than it would have if it was sitting
25 in an idle plant --

1 MR. SERINO: I think --

2 THE COURT: -- or it was being purchased for an idle
3 plant?

4 MR. SERINO: I think that the latter is relevant,
5 yes.

6 THE COURT: In other words, a hypothetical buyer is
7 going to spend more for an asset that they're going to use in
8 the business than for one they're going to put in a plant and
9 not use, aren't they?

10 MR. SERINO: I think that's absolutely right, Your
11 Honor.

12 THE COURT: So explain to me how you strip -- whether
13 you're supposed to strip out that additional value or how you
14 do it.

15 MR. SERINO: Okay. Well, I think there's no question
16 that a buyer who's going to use the equipment intuitively will
17 pay more than someone --

18 THE COURT: Of course it's going to be used to
19 generate income or cash flow.

20 MR. SERINO: Correct.

21 THE COURT: Right.

22 MR. SERINO: Okay. And that's why I think Rash says
23 under the replacement value world, assume that the buyer comes
24 from the debtor's business trade or situation. Now, but Rash
25 also says that you have to look at what the creditor has an

1 interest in. You have to assume that the buyer is buying
2 that -- the buyer here -- the creditor here does not have an
3 interest in the whole going-concern.

4 THE COURT: I understand that. But again, I use the
5 analogy of someone in the business is going to the PP&E
6 store --

7 MR. SERINO: Yeah.

8 THE COURT: And they're going to buy that PP&E that
9 they'll stick in a plant and operate, they're going to be
10 willing to pay more for it than if they're just going to stick
11 it in a plant and let the plant sit idle.

12 MR. SERINO: I think that's true, Your Honor.

13 THE COURT: Okay. So how do I --

14 MR. SERINO: And that's what Mr. Schmitt did. Mr.
15 Schmitt didn't look at --

16 THE COURT: Tell me how he did that. I really had a
17 lot of trouble following his testimony.

18 MR. SERINO: He didn't look at an idle plant or a
19 liquidated plant. He looked at a lights out plant. And what
20 that means is he said if I can't give credit for the working
21 capital and I can't give credit for the intellectual property
22 and I can't give credit for the intangible assets, what I've
23 got is a lights out plant waiting for somebody to buy that bare
24 naked PP&E and hit the switch. And I'm trying to figure out,
25 under Rash, what somebody will pay for that PP&E.

12

1 THE COURT: I understand that.

2 MR. SERINO: Okay. And so what he said, Your Honor,
3 is that that's not a liquidation scenario. And he was very
4 careful to say several times that he was not taking out of his
5 opinion the cost for any shutdown or maintenance in that
6 scenario.

7 And let me explain how he got to his number, Your
8 Honor. He did both a bottoms up and a cost -- he did a bottom-
9 up cost approach and a top-down approach. And we have on
10 Figure 3 is really his bottom-up approach. And he started with
11 the CRN, cost of reproduction new, what it would cost to
12 rebuild this PP&E --

13 THE COURT: Where in his testimony or his report did
14 he explain how he came up with that number?

15 MR. SERINO: This is Figure 3 from page 48 --

16 THE COURT: I know what it is. But where does he
17 explain where that number comes from or how it's computed?

18 MR. SERINO: I believe it's --

19 THE COURT: In other words, Mr. -- in comparison, Mr.
20 Beaton --

21 MR. SERINO: Yes.

22 THE COURT: -- said I went to the historical cross-
23 records and I looked at it and then I -- I guess I increased it
24 by some inflation factor using the PPI and that's how I got to
25 that number. Where is that --

1 MR. SERINO: Mr. Schmitt said the exact same thing in
2 his testimony, Your Honor. I can get you the pages. But he
3 said, what I did is I looked at every single piece of equipment
4 and I applied different PPIs to that piece of equipment and I
5 concluded that in 2008 dollars, it would cost 1.5 billion
6 dollars to replace that equipment. And then he said, I did a
7 similar analysis. And I said, what would it cost to replace
8 the capacity with new equipment. And he said, the cost was
9 only 754 million. And so that was the starting point. Nobody
10 was going to pay 1.5 billion --

11 THE COURT: Where did that 778,000 dollar deduction
12 come from?

13 MR. SERINO: That's the difference between the two.

14 THE COURT: I understand that. But where did it come
15 from?

16 MR. SERINO: Well, he concluded that when he was
17 trying to figure out the cost approach to valuation here.
18 You're not going to use 1.5 billion 'cause no one's going to
19 pay 1.5 billion if they can duplicate the capacity by buying
20 brand new equipment for 754 million.

21 THE COURT: But how did he reach the conclusion that
22 it was 754 million?

23 MR. SERINO: By going out and pricing things, by
24 looking at what it would cost to buy the equipment you need
25 today with today's technology to produce the same kind of

1 capacity that Wellman currently gets from its existing
2 equipment. It's as if he went out in 2008 and bought one
3 computer and said what do I need from this 2008 computer to get
4 from the old 2002 computer I was getting. It was more
5 efficient. The equipment's better. The equipment has better
6 capacity. He was able to do that for 754 million dollars. So
7 that became his starting point in his analysis. And then he
8 subtracted the physical and functional obsolescence.

9 THE COURT: How did he compute those?

10 MR. SERINO: The physical and functional
11 obsolescence? Let me see if I can refer Your Honor to a page
12 on that. Your Honor, I think in very general terms -- and I
13 don't have the page reference, I'm sorry. But in very general
14 terms, what he did is he compared the age of the relative
15 equipment for its physical obsolescence. Same thing Mr. Lerman
16 did. Mr. Lerman took physical obsolescence as well.

17 THE COURT: I understand that.

18 MR. SERINO: And what he did is he said a ten year
19 old car is going to be worth less than a one year old car
20 'cause it's got some physical obsolescence and physical
21 deterioration. And when he tried to do that for every piece of
22 PP&E --

23 THE COURT: But how did he know? What were the
24 assumptions he made? How did he come up with the number he
25 came up with? I understand the methodology. I think

1 everybody, in their mind, had the same methodology. But how
2 did he come up with the number he came up with?

3 MR. SERINO: For physical obsolescence?

4 THE COURT: For the two obsolescence deductions.

5 They aggregate 630 million or 640 million dollars. It's a lot
6 of money.

7 MR. SERINO: I admit I'm probably just not explaining
8 this well, Your Honor. I know the methodology was that he
9 took --

10 THE COURT: In other words, let me go back to Mr. --

11 MR. SERINO: Yeah.

12 THE COURT: He said he looked at computerized
13 valuation guides --

14 MR. SERINO: Right.

15 THE COURT: -- for every piece of equipment, at least
16 for the machinery and the equipment. He did something
17 different from the real estate and that's the number he came
18 out with. I don't recall Mr. Schmitt giving the same
19 testimony. In other words, he said this was his result but he
20 didn't really -- I don't recall him explaining precisely how it
21 is he got to that result.

22 (Pause)

23 MR. SERINO: And I think -- Mr. Dexter is giving me
24 some help. His recollection is the same as mine is that what
25 he did -- what Mr. Schmitt, we thought, testified to, and we'll

1 try to get the transcript, is he compared the age of the actual
2 equipment, when he took the bottoms up approach and looked at
3 every single piece and then he prepared the value of that
4 equipment as is and then he tried to look at the value of that
5 equipment with its assumed useful life.

6 THE COURT: What assumptions did he make regarding
7 useful life? One of the problems I have here and I have it
8 with some of the other valuations is I'm just being given a
9 number and the methodology is being explained. But there isn't
10 necessarily a clear explanation of what they assumed and how
11 they got to that number. And obviously, following the same
12 methodologies, at least Lerman and Schmitt came up with wildly
13 disparate results.

14 MR. SERINO: Right, Your Honor. And I think one of
15 the reasons is maybe we skipped over some of that in the direct
16 exam because it's in that 350-page report.

17 THE COURT: Well, you got to point me to it because
18 I'm not going to sit there and read a 350-page --

19 MR. SERINO: I know. And I'll start -- I'll --

20 THE COURT: -- report, most of which is boiler plate.
21 But that's something else.

22 MR. SERINO: I know. And I'll dig that out. But I
23 think the point I would make is you're absolutely right that
24 Mr. Lerman and Mr. Schmitt came out wildly at disparate ends of
25 the spectrum. But Mr. --

1 THE COURT: And that's why I started by asking you
2 what are the components of their analysis that caused this
3 disconnect?

4 MR. SERINO: Well, what I was going to say, Your
5 Honor, is Mr. Schmitt and Mr. Beaton came out very close
6 together. It was 74.3 million for Mr. Beaton --

7 THE COURT: We'll get to Mr. Beaton later.

8 MR. SERINO: -- 70.8 million for Mr. Schmitt. And
9 what I was going to say is this is -- this Figure 3 is Mr.
10 Schmitt's answer to Mr. Beaton's bottom-up approach. And I
11 think the approach was very similar. What they did is they
12 looked at what it would cost to replace the capacity today,
13 they applied some penalty for physical and functional
14 obsolescence, they came up with an assumed earnings value of
15 the equipment. And then Mr. Schmitt also did the same thing to
16 the real estate. He came up with an assumed earnings value for
17 the real estate. And then he needed to know whether that real
18 estate and that equipment would suffer from any economic
19 obsolescence, whether it should be penalized for external
20 factors.

21 THE COURT: Explain to me how he computed that 62.29
22 percent --

23 MR. SERINO: Okay.

24 THE COURT: -- and what assumptions he made.

25 MR. SERINO: Well, what he did, Your Honor, is this

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1 is kind of the intersection between the bottom-up and the top-
2 down. And what he did is he said let me do my top-down
3 analysis. I come with a business enterprise value of 273. I
4 subtract out 173 for working capital. I subtract out 28.5 for
5 intangible assets and I add 170,000 for a Johnsonville
6 adjustment. I get a replacement value of the PP&E of 70.8
7 million dollars. And then he said I need to compare that
8 actual replacement value with the assumed earnings value that
9 I've gotten in my bottom-up approach.

10 And so he looked at the 70.8 million dollars and he
11 said, of that 70.8, 7.9 has already been taxed for economic
12 obsolescence. 7.9 of the valuation is being from external
13 sources where Mr. Schmitt could say it's like a blue book
14 value. It's already been taxed for economic obsolescence. So
15 he subtracts that out. He subtracts -- from 70.8 he takes out
16 7.9. That leaves him with actual PP&E replacement value of
17 about sixty-three million. He compares that to the assumed
18 PP&E replacement -- assumed PP&E value of 166 million. That's
19 the 120 -- it's the 120 for the machinery and equipment and
20 forty-six for real property. And he says sixty-three million
21 minus 166 million of the assumed means a negative 103. And to
22 put that into a percentage, he takes the negative 103, divides
23 it by the assumed earnings of 166 and says the economic
24 obsolescence is 62.29 percent. He then takes that 62.29
25 percent economic obsolescence penalty, applies it to the

1 assumed machinery and equipment valuation, adds back the
2 portion of this that he had taken out before, the portion of
3 7.9, adds back 4.4 here, he adds back the balance on the real
4 estate side, the 3.5 on the real estate side, and he comes up
5 with 49.8 for replacement value of the equipment, 20.9,
6 replacement value of the real estate and 70.8, the total
7 replacement value. This is the cost approach and it flips with
8 his top-down approach.

9 THE COURT: Comes up with the exact same number.

10 MR. SERINO: Your Honor --

11 THE COURT: Was that a coincidence?

12 MR. SERINO: You know, I don't think it is a
13 coincidence. I think it's an indication of the reliability of
14 his work product. And that's not the only indication. I think
15 what we saw is when he did the top-down approach, he came up
16 with 273 million dollars, 260 for the chemical and thirteen for
17 Johnsonville. Now, he did multiple valuations. He did a DCF,
18 which was 245, he did a market guideline approach -- a
19 guideline public company approach, which came out at, I think,
20 260, and he did a -- 275. He did a market -- M&A approach of
21 260. Now they were all very close, Your Honor. 245, 260, 270.
22 They were all very close. But it's not as if he had one
23 dependant on the other. He did three separate analyses. And
24 they all came out very close. And I think that's an indication
25 of how reliable his work product is. And that's not the only

1 indication.

2 THE COURT: Well, you know, Mr. Lerman came out close
3 with two or three methods also.

4 MR. SERINO: Well, we're going to --

5 THE COURT: Is that an indication of the reliability
6 of his approach?

7 MR. SERINO: Well, we're going to get to the
8 methodological errors in Mr. Lerman's approach that you didn't
9 hear about Mr. Schmitt.

10 THE COURT: Okay.

11 MR. SERINO: But, Your Honor, on this -- I think you
12 raise an excellent point about the results being consistent
13 because here's a good variable.

14 THE COURT: They're identical; they're not
15 consistent.

16 MR. SERINO: And here's a good variable to apply to
17 that, Your Honor. Here's a good variable to apply to that.
18 There was testimony that in April and March of 2008, Wellman
19 received bids for this business from competitors where the
20 proverbial bundle of sticks. And where do those bids come in
21 at?

22 THE COURT: 260 million dollars.

23 MR. SERINO: Exactly right. 260 million dollars.
24 And Mr. Schmitt was right on the money but he did not bake
25 those bids into the equations. He didn't use them in as

1 computative. He was at 260 before he added in Johnsonville.
2 Right on the money.

3 So, is it a coincidence? I don't know, Your Honor.
4 I think it's an indication of how reliable he is.

5 THE COURT: Wasn't the debtor under a compulsion to
6 sell?

7 MR. SERINO: No, Your Honor. That's the insinuation
8 that the first liens are trying to drive home. That's not what
9 the evidence is. You remember Mr. Yearley from Lazard? He
10 took the stand and he told us about that process. And he said
11 forget about the debtors' perspective. I can tell you that
12 from the buyer's perspective, there was a competitive and
13 exhaustive process. Market participants were given all the
14 information they needed and they made a best and final bid.
15 And Mr. Yearley said not only that, Your Honor, the market
16 participants wanted those assets and, just as badly, they
17 wanted to make sure those assets didn't fall into the hands of
18 their competitors. That's why this was not a distressed bid.
19 This was a very real bid and a final bid.

20 Mr. Yearley also said -- he had another answer to an
21 insinuation the first liens were making. The first liens said
22 well, if this bid was so great, why didn't you take it,
23 Wellman. And Mr. Yearley had an answer for that. It's a red
24 herring. Wellman never got to decide whether they were going
25 to take the bid or not because the creditors BKed it before it

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1 got to that point. The creditors told Wellman they wouldn't
2 support that bid. And so Wellman had to make a bankruptcy, a
3 strategic bankruptcy decision to pursue reorganization rather
4 than the bid process.

5 Now, Your Honor, I suppose that the first liens are
6 going to argue that Mr. Schmitt made a mistake by doing the
7 lights-out approach, similar to the question Your Honor was
8 asking not too long ago. And I want to address that because I
9 think it's important and maybe I've done a bad job of
10 articulating why his lights-out approach is perfectly
11 consistent with Rash. He said the lights-out approach, which I
12 think is similar to the bare naked PP&E that the first liens
13 embraced in their opening and then Mr. Lerman ran from in his
14 analysis -- Mr. Schmitt said that the lights-out approach is
15 not a liquidated plant. The lights-out approach is what you
16 get when you separate from the PP&E the working capital,
17 intellectual property and the intangible assets. You're left
18 with bare naked PP&E. There's nobody to run it. There's no
19 capital to feed it. There's no intellectual property to drive
20 it. And that's why he did a lights-out approach. But he was
21 very careful to say I didn't tax them for shut-down or
22 maintenance cost during that lights-out approach. Mr. Schmitt
23 did that because he thought that's what Rash asks him to do.
24 Rash says you look here at the PP&E because that's what the
25 firsts have a lien in and nothing else. Rash says you don't

23

1 give the creditor credit for modifications to their collateral
2 package if they don't have a lien on that. And this was not
3 Mr. Schmitt reinventing the wheel. He has done this. This is
4 not novel for him to take away going-concern value from an
5 asset. He's done it hundreds of times for asset-based lenders,
6 he had testified.

7 And that's exactly what he did here, Your Honor. He
8 assumed that this PP&E would be bought by someone who wanted to
9 operate it. But what he did that Mr. Lerman didn't do is he
10 tried to follow Rash by stripping out the going-concern value
11 and saying what is that bare naked PP&E worth. That's what he
12 did and he's done it hundreds of times before.

13 THE COURT: I have another question. In the debtors'
14 disclosure statement, it valued, on a liquidation basis, the
15 PP&E at sixty-six million dollars.

16 MR. SERINO: Correct.

17 THE COURT: And Mr. Schmitt is valuing the PP&E on a
18 going-concern basis at seventy or seventy-one million dollars.
19 That sounds awfully close.

20 MR. SERINO: It does, Your Honor, but Mr. Schmitt had
21 an answer for that, too. If you'll recall, Mr. Schmitt
22 testified -- I think the liquidation value is sixty-five or
23 sixty-six million. And Mr. Schmitt said, well, first of all,
24 that's apples to oranges. I did not do a liquidation analysis.
25 But then he said --

1 THE COURT: What's the difference? What assets are
2 included or excluded from the liquidation analysis that are in
3 his analysis?

4 MR. SERINO: It was a different value -- it was
5 similar assets; a different valuation approach. Mr. Schmitt
6 used replacement valuation. But it was not a sixty-six to
7 seventy comparison. Remember, Mr. Schmitt said that sixty-six
8 or sixty-five isn't taking into account ten million dollars in
9 costs.

10 THE COURT: Yeah, but we don't care about the costs
11 in a going-concern value --

12 MR. SERINO: Well, in a go

13 THE COURT: -- cause those are liquidation costs,
14 aren't they?

15 MR. SERINO: They were liquidation costs that need to
16 be subtracted from that sixty-six to see what the company's
17 real liquidation value is.

18 THE COURT: Why?

19 MR. SERINO: And it ended up to be fifty-five. That
20 was Mr. Schmitt's testimony.

21 THE COURT: If there were no selling costs then the
22 liquidation value is sixty-six million. Why doesn't that
23 compare to the seventy million which doesn't have liquidation
24 costs?

25 MR. SERINO: I mean, all I can tell you, Your Honor,

1 is what Mr. Schmitt's answer to that was.

2 THE COURT: Yeah, but --

3 MR. SERINO: His answer was that the premise of
4 liquidation has to assume that there's selling costs involved.
5 And that ten million dollars, he said, you take that out of the
6 sixty-five million, you get fifty-five million. Now you're
7 fifteen million dollars, or twenty-five percent, less in his
8 replacement value analysis.

9 (Pause)

10 THE COURT: Go ahead.

11 MR. SERINO: I think the other thing the first liens
12 may make a point of, Your Honor, and you've covered most of
13 them already, is that --

14 THE COURT: I have questions for them, too.

15 MR. SERINO: -- is the impairment write-down. I
16 think the first liens have insinuated that Mr. Schmitt's
17 valuations can't be trusted because they are still
18 significantly less than Wellman is carrying the PP&E on its
19 books after the impairment write-down. But, again, this is an
20 apples to oranges comparison. Let me explain what I mean.
21 You'll recall Mr. Phillips, the CFO of Wellman, testified and
22 he said two things that are critical here: one, the company's
23 definition of PP&E on its financial statements is much broader,
24 much more inclusive than the collateral package of the first
25 liens' PP&E. And, two, he said, what drove the impairment

26

1 write-down was the trading value of the debt and the equity as
2 of December 31, '07. What Mr. Schmitt's doing is the
3 replacement value of the PP&E not as of December 31, '07 but as
4 of September 30, 2008.

5 Let me, Your Honor, just address Mr. Lerman's
6 opinions because I think Your Honor's got to figure out which
7 of these valuation opinions is the most reliable and which is
8 most close to Rash. And you've raised some questions about Mr.
9 Schmitt. Let's talk about Mr. Lerman. I've already talked
10 about why I think he deviated from Rash and why I think he
11 credited the PP&E with going-concern elements that they do not
12 have a lean on. But severe methodological errors. He
13 testified that his DCF model was his best model. It's the one
14 he has the most confidence in and the most reliance on. Yet,
15 let's review some of the errors he made there, some of the
16 errors. He said that his numbers and projections were more
17 conservative than Wellman's. Yet we saw that he projected
18 gross profit margins in 2008 that were ten to sixteen times
19 Wellman's historical margins from 2007. And he projected gross
20 profit margins in a terminal year into perpetuity that were two
21 to three times what Wellman was projecting. Greatly overstated
22 the gross profit margins that Wellman could be expected to
23 earn.

24 Mr. Lerman assumed a three percent growth rate from
25 2012 through perpetuity despite the fact he had to admit that

1 at that rate, Pearl River would exceed capacity in about eight
2 years. He's got them add in another three percent above
3 capacity for the rest of --

4 THE COURT: But in the end of the day, Mr. Schmitt, I
5 think, projected higher level of net income over the four or
6 five-year period than Mr. Lerman did. And so the question is,
7 how did Mr. Lerman wind up with a higher cash flow and
8 therefore a higher valuation.

9 MR. SERINO: Well, I think, first of all, Mr. Schmitt
10 relied on the company's projections; Mr. Lerman did not. And I
11 think the reason why Mr. Lerman ended up with a higher cash
12 flow is because he didn't deduct for any corporate overhead
13 expense, he didn't assume any state income taxes. But the big
14 one was he assumed a forty-two million dollar depreciation for
15 the terminal year into perpetuity against capital expenditures
16 of only two million dollars.

17 THE COURT: Um-humm.

18 MR. SERINO: It was a forty-million dollar delta
19 there. And he said that's my assumption. And I said, well,
20 what if the book value of those depreciable assets is only two
21 forty. Won't they be gone in six years? He said yes.

22 THE COURT: Well, one of the things that Mr. Schmitt
23 assumed over the four or five-year period is almost an eighty
24 million dollar negative change to net working capital. What
25 was the basis for that assumption? That had an enormous effect

1 on the difference in the valuations.

2 MR. SERINO: I think that that assumption -- it was
3 due to the fact, Your Honor, that Mr. Schmitt was assuming
4 growth --

5 THE COURT: Right.

6 MR. SERINO: -- and Mr. Lerman wasn't, additional
7 capital expenditures, and the need to assume for additional
8 working capital.

9 THE COURT: This wasn't capex. This was just a
10 change in, I guess, an increase in the accounts receivable --

11 MR. SERINO: And I thought that was just a function
12 of Mr. Schmitt's assumption that there will be continued growth
13 in the terminal year through perpetuity.

14 THE COURT: That's a big number. And that has a
15 drastic effect on the valuation. And that's an add-back for a
16 cash flow --

17 MR. SERINO: Hang on a second, Your Honor.

18 THE COURT: -- or a subtraction in this case.

19 (Pause)

20 MR. SERINO: I was getting some help from the
21 Wellman --

22 THE COURT: Okay.

23 MR. SERINO: -- CFO because these numbers, again,
24 that Mr. Schmitt used came from Wellman. And what Mr. Phillips
25 tells me is that Wellman increased its projections because

1 prices were going up and because inflation, five percent. And
2 so they brought up the cost of their inventory --

3 MR. PHILLIPS: Inventory receivables.

4 MR. SERINO: Inventory receivables.

5 THE COURT: Okay. Go ahead.

6 MR. SERINO: Your Honor, and I did want to -- I
7 wanted to stay with Mr. Lerman on this problem he had where he
8 had depreciation exceeding capital expenditures and perpetuity
9 because not only was that inconsistent with the book value of
10 the assets but you remember Mr. Qureshi put one of the treaties
11 in front of him on valuation.

12 THE COURT: Treatises.

13 MR. SERINO: Treatises. I think it was Mr.
14 Hitchner's treatises that said that this situation where you
15 have depreciation that exceeds capital expenditures, Mr.
16 Hitchner said is "a common mistake" and is "an obviously
17 impossible situation". And you'll notice, Your Honor, that Mr.
18 Lerman's errors were confined to the DCF model. There were
19 also errors on his market approach model as well. We heard
20 that, for instance, he assumed the same useful life for
21 Palmetto and Pearl River, thirty-five years, even though Pearl
22 River was three times older than Palmetto at the time.

23 We heard that Mr. Lerman did not get to see the bids
24 that Wellman received in March or April, the 230 to 260 million
25 dollar bids despite asking first liens' counsel for the same.

1 And those bids were hundreds of millions of dollars less than
2 his business enterprise value.

3 And most importantly, Your Honor, we heard that Mr.
4 Lerman sat down and thought about economic obsolescence and
5 concluded that there would be none. He thought that there
6 would be no external factors that would create any economic
7 obsolescence, not the rising cost of raw materials, not the
8 rising cost of energy, nothing. Zero. He didn't tax for any
9 economic obsolescence. And so we said, what's your basis for
10 that? And he said, well, I read a contract or two in Wellman's
11 data room. And then we said, well, what other facts did you
12 see. Did you see the fact that Wellman's historical cost of
13 sales percentage had been going up? Yes, I did. Did you see
14 the fact that Wellman's price paid for raw materials had been
15 going up? Yes, I did. Did you see the fact that Wellman's
16 historical gross margins were going down? Yes, I did. Did you
17 read every single contract for every customer? No, I didn't.
18 And yet that confluence of factors never caused Mr. Lerman any
19 doubt in his assumption that Wellman could pass on a hundred
20 percent of its cost, as raw material cost, to customers. And
21 Mr. Phillips testified the fact of the matter is, Wellman
22 cannot pass on its raw material increased cost to seventy
23 percent of its sales.

24 Now, Mr. Lerman never asked that question, Your
25 Honor, and that's troubling. That means, he either didn't

1 figure it out or he didn't want to know the answer. He didn't
2 want to know that those one or two contracts were not
3 indicative of the entire business and that some economic
4 obsolescence might be appropriate. And if you started to hit
5 his numbers with thirty, forty, fifty percent economic
6 obsolescence, it would fall down dramatically.

7 And that brings me to another issue about Mr.
8 Lerman's testimony, Your Honor, and that's credibility. He
9 testified that his DCF model was his most confident. He
10 testified that he never relied on Wellman's projections. Yet,
11 every time he got into a tough spot on cross-examination about
12 that DCF model, he said, well, those numbers came from Wellman
13 or Wellman didn't give me the numbers I needed. Now, if that's
14 the case, Your Honor, how can this model be the one he's most
15 confident in? If that's the case, how come he testified, at
16 page 184 of his deposition, that "Wellman provided me with
17 great detailed information and I mean a lot of information".
18 If that's the case, how come the other two experts who were
19 given access to identical information didn't have this problem?
20 And most importantly, Your Honor, ask yourself this. If that's
21 really the case, how come Mr. Lerman did a valuation report,
22 two supplements to that report, sat through a day and a half
23 deposition, sat through a two-hour direct examination and never
24 mentioned this issue until cross-examination.

25 I don't think that adds up, Your Honor. But even if

1 you credit Mr. Lerman at face value, that he didn't get the
2 information he thinks he needed or he got the wrong the
3 information, it just means his work is not reliable. Maybe
4 it's not even through any fault of his own. But he should have
5 spoken up before cross-examination. If he's saying I didn't
6 get the right numbers or I got the wrong numbers or I didn't
7 get the information, it means he doesn't have confidence in his
8 result.

9 And, Your Honor, that's really the bottom line here.
10 And I will -- if you want us to brief this more to answer those
11 specific questions, I'm happy to do it because I know that's
12 important. But I think, high level, if you look at it, three
13 appraisers went out and they were given the exact same
14 standard, they were given the exact same information and they
15 were asked to apply that standard to the same PP&E. Two of
16 them came back within shouting distance of each other: Mr.
17 Schmitt at 70.8 independently; Mr. Beaton at 74.3. And one of
18 them came back at 136.8, Mr. Lerman, the outliner. And I don't
19 think that's a coincidence, Your Honor.

20 It's not a coincidence that Mr. Schmitt and Mr.
21 Beaton have the highest credentials one can get in the American
22 Society of Appraisers. Mr. Lerman's not even recognized by the
23 ASA. It's not a coincidence that before this trial Mr. Lerman
24 had never been qualified to testify as an expert witness while
25 Mr. Beaton and Mr. Schmitt had been qualified many times. We

1 brought that up for a reason. Not to pile on to Mr. Lerman but
2 to show that it was his lack of experience, his lack of
3 credentials, his lack of qualifications that manifested
4 themselves here in these common errors, in these misassumptions
5 that he made in his valuation projections. And that's why,
6 Your Honor, at the end of the day, you can't rely on his 136.8
7 million conclusion of value. The right answer has got to be
8 either Mr. Schmitt's 70.8 million dollar conclusion of value or
9 Mr. Beaton's 74.3 million dollar conclusion of value. Thank
10 you, Your Honor.

11 THE COURT: Thank you.

12 MR. QURESHI: Good afternoon, Your Honor. For the
13 record, Abid Qureshi, Akin, Gump, Strauss, Heller & Feld on
14 behalf of Wilmington Trust as the second lien agent.

15 Your Honor, if I may hand up a couple of
16 demonstrative exhibits for closing, I think it would be
17 helpful in terms of --

18 THE COURT: Sure. Thank you.

19 MR. QURESHI: Now, Your Honor, what I propose to do
20 in closing is really three things. First and foremost, answer
21 the Court's questions beginning with the question that actually
22 began my opening argument with; second, to explain Mr. Beaton's
23 testimony and why we think he did it the right way; and third,
24 to revisit, again without repeating too much of what you heard
25 from Mr. Serino, Mr. Lerman's failings.

1 Now, Your Honor, what I'd like to start with is the
2 very first demonstrative exhibit in the tabs that I just handed
3 up to you which is Mr. Beaton's triangle. That's tab 1. Your
4 Honor --

5 THE COURT: I think it's a pyramid.

6 MR. QURESHI: Pyramid. And as Your Honor may recall,
7 that is the pyramid that Mr. Beaton drew on the board during
8 his direct examination. Now, Your Honor asked at opening and
9 asked Mr. Serino again now, isn't it the case that this PP&E is
10 worth more to somebody who is going to operate it than it is to
11 somebody who is not. And that is absolutely the right question
12 to ask. And the answer is --

13 THE COURT: That's what you told me the last time,
14 too.

15 MR. QURESHI: That is what I told you last time.

16 THE COURT: At least you're consistent.

17 MR. QURESHI: And the answer, Your Honor, is yes,
18 that that person is going to value it more now. I think --

19 THE COURT: And how do we -- let me -- you know, a
20 lot of this is that you can't -- in the going-concern value,
21 you have to strip out the elements that they don't have a lien
22 in. On the other hand, a going concern, from what you've just
23 said and what other question I asked, enhances the value of any
24 particular asset 'cause it's going to generate income in an
25 operating business. So how do you separate those two?

1 MR. QURESHI: Your Honor, I think one needs to
2 distinguish between going-concern value and valuing assets on a
3 going-concern basis. Recall that Mr. Beaton explained his
4 premise of value when conducting his analysis was valuing these
5 assets on a going-concern basis.

6 If you look at the pyramid with PP&E on the bottom,
7 working capital and general intangibles, we take it all
8 together. When all of those pieces are operating together,
9 that generates going-concern value. In other words, the sum of
10 the three things independently is not going to be the whole.
11 The whole will be more. We cited a bunch of cases in our
12 opening brief for the proposition that going-concern value is
13 an intangible asset. I don't think there's any dispute there.
14 I have not seen a case to the contrary --

15 THE COURT: But what does that mean in terms of
16 valuing PP&E that's going to be used in a going concern?

17 MR. QURESHI: What that means, Your Honor, is that
18 when all three of the elements of this pyramid are operating
19 together they are generating going-concern value, that value
20 belongs to the second lien holders. But when the PP&E on its
21 own is being valued on a going-concern basis, which everybody
22 agrees is the right approach, you're not liquidating and not
23 foreclosure but going-concern basis, what that means is, again,
24 how Mr. Beaton assumed it. He assumed that the hypothetical
25 buyer would come with all of these pieces --

1 THE COURT: Right.

2 MR. QURESHI: -- with the working capital, with the
3 general intangibles and would, in fact, operate. And so, he
4 valued it on that basis. Now that gives the first lien holders
5 the benefit of a going-concern premise of value.

6 Now, distinguish that from a liquidation approach.

7 Mr. Beaton explained that in his going-concern premise of
8 value, there is an assemblage of assets. It's all together;
9 it's all in the same location. It's going to stay there. And
10 this equipment is going to continue to make the very same
11 product that Wellman is making today. That is a completely
12 different universe from a liquidation. In a liquidation, one
13 assumes that that equipment is going to get broken down. It's
14 going to get sold in bits and pieces. Those pieces that can be
15 moved might have more value than those pieces that can't be
16 moved. Mr. Beaton called it separating marketable from semi-
17 marketable from nonmarketable. And the nonmarketable
18 essentially is sold for scraps.

19 Now, Your Honor also asked Mr. Serino, well, isn't it
20 troubling that you have the conclusion of value of either Mr.
21 Beaton or Mr. Schmitt of seventy to seventy-four and a
22 liquidation value by Lazard of sixty-six depending on the
23 number. And I agree with Mr. Serino on this point, Your Honor.
24 And that is that the right comparison -- for purposes of
25 inquiring into Your Honor's question, which is shouldn't I be

1 troubled that the liquidation value is so close to the
2 replacement value that these experts found, the right
3 comparison is not sixty-six. Page 55 -- because if there was a
4 liquidation, if these assets were liquidated, there's no
5 question that costs would be incurred. And Lazard has
6 estimated those costs at approximately eight million dollars so
7 that the right comparison is in fact fifty-five million.

8 THE COURT: I agree with you that that would be the
9 proceeds of the liquidation.

10 MR. QURESHI: Right.

11 THE COURT: But in terms of the value of the PP&E,
12 somebody is still valuing it for liquidation purposes before
13 costs at sixty-six. And why isn't that the appropriate
14 comparison?

15 MR. QURESHI: Your Honor, I think --

16 THE COURT: Let me ask you. Assuming that it is the
17 comparison, should I be troubled by it?

18 MR. QURESHI: I don't think you should be troubled at
19 all.

20 THE COURT: Tell me why I shouldn't be troubled.

21 MR. QURESHI: Why you shouldn't be troubled is
22 because going-concern value, that is, if -- again, you're going
23 to take this pyramid and keep it all together functioning today
24 with all the benefits, the intangible benefits that that
25 creates, again, under our going-concern value, it would lead to

1 a higher value than Mr. Beaton's conclusion. And the
2 difference between that value and liquidation would be much
3 greater.

4 THE COURT: I don't think I understand that. It
5 sounds to me like what you're saying is that someone who's in
6 the business and not going to use the equipment would pay the
7 same as someone who is not in the business and -- I'm sorry,
8 someone who's in the business and will use the equipment is
9 going to pay the same as someone who's not in the business and
10 won't use the equipment.

11 MR. QURESHI: No, Your Honor. I agree that somebody
12 who's in this business is going to pay more for these assets
13 than somebody who's not. There's no question about that.

14 What --

15 THE COURT: But based on the evidence in this case,
16 it appears that it's only going to be about eight million
17 dollars what your expert --

18 MR. QURESHI: Eight million dollars over the total
19 liquidation.

20 THE COURT: Yeah.

21 MR. QURESHI: Well, Your Honor, I think the way to
22 approach it is this. So, everybody agrees that all we're
23 trying to place a number on is the PP&E.

24 THE COURT: That's all we're trying to do.

25 MR. QURESHI: That's all we're trying to do.

1 THE COURT: That sounds pretty simple.

2 MR. QURESHI: And so, again, Mr. Beaton did that

3 assuming that these other elements would exist. They would be

4 held by the buyer. This would be the buyer in the industry who

5 is going to have intangibles, who is going to bring working

6 capital. There are costs to doing that, Your Honor. Again,

7 because the first lien holders are not entitled to the benefit,

8 to the value of the intangible assets that belong to the second

9 lien holders. There is going to be a cost associated with

10 taking the PP&E value -- on a going-concern basis on the bottom

11 of this pyramid and layering on top of it working capital and

12 layering on top of that all of the intangibles that you need to

13 run the business. And this is where we get into Mr. Beaton's

14 various deduction factors. What he tries to do is isolate what

15 that cost is. And again, the reason he has to do that is

16 because if you just value the whole thing then the first lien

17 holders gets the benefit of our collateral because the whole

18 thing captures going-concern value.

19 THE COURT: But he didn't do that. Or at least he

20 didn't purport to do that.

21 MR. QURESHI: That's correct. He did not do that.

22 He, again, just valued the PP&E for that very purpose so that

23 he wouldn't attribute to the first lien holders value that

24 attaches to intangibles. And so, again, the two pieces on the

25 top of pyramid that the hypothetical buyer needs to layer on,

40

1 there's a cost involved in that. There's a cost, as Mr. Beaton
2 explained, with customer contacts, prior relationships, work
3 force, software, which is also a subject of the second lien
4 holders' liens, all of those things take time and cost money.
5 And that's what goes into the deduction factors that Mr. Beaton
6 applied to arrive at this concluded value.

7 THE COURT: Well, let's talk about his specific
8 economic deduction, his deduction for selling at holding costs
9 which, in the aggregate, it was seventy-five percent of his
10 depreciated replacement costs. He said that it was
11 unscientific. He said it was somewhat subjective. Why
12 seventy-five percent? Why not sixty percent? Why not forty
13 percent?

14 MR. QURESHI: Your Honor, I think --

15 THE COURT: It makes a big difference.

16 MR. QURESHI: It makes a very large difference, no
17 question about that. And in his -- for each of those two
18 specific obsolescence categories, it was fifty percent for each
19 one and I think a total of -- in the range of 200 million
20 dollars deduction.

21 THE COURT: Seventy-five percent of the depreciated
22 replacement cost.

23 MR. QURESHI: That's correct, Your Honor. And every
24 valuation expert, at various stages in the process, apply
25 subjective judgment. Mr. Lerman, I think, did it more than

1 others because his subjectivity is in the numbers themselves.
2 But what Mr. Beaton did is -- and, Your Honor, the slides that
3 you have before you, Slide 3 to Slide 4, set out the various
4 categories and information that he considered. But Your Honor
5 is absolutely right. Mr. Beaton was clear. There is no
6 mathematical formula. Sure, he could have said my economic
7 obsolescence is 48.79 percent. That would have been no more
8 based on a mathematical formula than the fifty percent that he
9 arrived at. At the end of the day, to borrow a phrase that Mr.
10 Beaton used, this is where appraisers earn their dollars. It
11 is the application of their judgment and their experience in
12 considering all of these factors through which they arrive at a
13 specific deduction. And we cannot hide from the fact, Your
14 Honor, that there is no mathematical formula. And none of the
15 experts here arrived at their conclusions purely through the
16 application of a mathematical formula. There is judgment at
17 all points.

18 I think what Your Honor should focus on is the extent
19 in which those judgments are based on and supported by
20 objective information or based on diligence that was conducted
21 or based on marketed information. And I think that's what Mr.
22 Beaton did to arrive at his deduction factors.

23 Does Your Honor has any specific questions about that
24 that I can answer?

25 THE COURT: Did Mr. Beaton have to value the

1 intellectual property or the intangibles?

2 MR. QURESHI: He did not.

3 THE COURT: Okay. But if you look at his selling and
4 holding costs, everything that he's backing out looks like it
5 fits his definition of intangibles.

6 MR. QURESHI: What he's backing out of here, Your
7 Honor, is the costs that the hypothetical buyer would incur in,
8 again, looking back at the pyramid, bringing these two elements
9 on top --

10 THE COURT: But isn't that another way of saying,
11 he's valuing the intangibles?

12 MR. QURESHI: I don't think so, Your Honor. He did
13 not -- there are --

14 THE COURT: I know he didn't use that phrase.

15 MR. QURESHI: Right.

16 THE COURT: But isn't that what he's doing?

17 MR. QURESHI: I don't think that is what he's doing,
18 Your Honor. Again, these are certified appraisers. He did his
19 work in accordance with the USPAP guidelines. And those
20 guidelines have a very specific way of how you value
21 intangibles, how you value a royalty streamer on a patent, how
22 you value trademarks, how you value customer relationships, how
23 you value --

24 THE COURT: But he didn't use any of these.

25 MR. QURESHI: He didn't do any --

1 THE COURT: He just used an assumption.

2 MR. QURESHI: He didn't do any of that. And so he,
3 again, did not support the value of the intangibles at all. He
4 said the most direct approach to get to my numbers for the PP&E
5 doesn't require that I do that. But these factors --

6 THE COURT: But didn't he really do that when he
7 backed -- what I'm saying is look, he backed out key selling
8 costs and he essentially -- the selling and holding costs, most
9 of which are the intangibles, which come out to seventy-four
10 million dollars on his analysis. Actually, if he backed them
11 out first, it would have been 148 million. But --

12 MR. QURESHI: I --

13 THE COURT: None of the other experts valued the
14 intangibles at that amount.

15 MR. QURESHI: Well, again, I think, Your Honor,
16 they're coming at it from two different perspectives. The
17 other experts both purported to value the intangibles which is
18 something that Mr. Beaton did not do. Now, what he is trying
19 to capture --

20 THE COURT: What I'm saying is I disagree with you.

21 MR. QURESHI: I understand that.

22 THE COURT: I think he did do that indirectly.

23 MR. QURESHI: Then let me try to explain why --

24 THE COURT: Okay.

25 MR. QURESHI: -- I don't think he did, Your Honor.

1 And it's this. That what he's selling at holding costs are
2 really trying to capture is not value but cost. And so for
3 example, he testified that some amount of time would be
4 required for a buyer from the day that they purchased the PP&E
5 until it's up and running. Well, they own the plant at that
6 point so they laid out a bunch of money to buy the PP&E and
7 it's not very -- there are costs associated with hiring a bunch
8 of people to reinstall software, to reprogram machines because,
9 again, the software doesn't belong to the first lien lenders,
10 and there's, most significantly, lost profit for a period of
11 time. Now the experts differ as to what is that period of
12 time. The first lien said anywhere from zero time to sixty
13 days. And Mr. Beaton has testified that it would be a little
14 longer than that, in his estimation somewhere from three to six
15 months.

16 THE COURT: I thought he -- Mr. Lerman testified that
17 after Hurricane Katrina -- I don't remember which one of the
18 plants it was but it was up and running in sixty days.

19 MR. QURESHI: Oh. Sure. That was the Johnsonville
20 or the Pearl River plant.

21 THE COURT: Well, whatever it was.

22 MR. QURESHI: Whatever plant it was. And no dispute
23 there. But, Your Honor, rebuilding the bricks and mortar which
24 is what happened when that plant was destroyed by the hurricane
25 has nothing to do with what's going to happen here because --

1 THE COURT: And losing the labor force?

2 MR. QURESHI: Well, losing the labor force certainly
3 would be one component. But, Your Honor, here what we're
4 talking about -- I mean, customer relationships, supplier
5 relationships, software. I mean, we have a lien on the
6 software. There's no dispute that we have a lien on that. And
7 even the first liens' expert agrees that there's going to be
8 time and delays involved in getting engineers and some
9 technicians into these plants to reinstall that software or to
10 reprogram the machine. There was also testimony, Your Honor,
11 that Wellman operates these machines in a different way from
12 its competitors. They don't take a production line from
13 Buehler or from Zimmer and just plug it in and press go. It
14 operates through their know-how and through the know-how of
15 their engineers and the expertise of their engineers. And
16 again, that's all something that when you assume that the
17 intangibles are going to be gone, there's a cost and a time
18 element involved in that.

19 So, to come back to your question which is didn't
20 Beaton really value the intangibles, I really think, Your
21 Honor, that he comes out from the other side which is the cost
22 and not the value of the two.

23 Now, Your Honor, just a few more points on what Mr.
24 Beaton did do, if I may. So again, he began his analysis with
25 every single piece of equipment in every building in every one

1 of those plants. I think he testified that there's more than
2 6,000 individual pieces of equipment in total. So, yes, it is
3 the case that his specific deduction factors are not based on a
4 mathematical formula but there is a lot of objective data that
5 went into Mr. Beaton's analysis. And I don't think that can be
6 said equally for Mr. Lerman.

7 So, unless Your Honor -- does Your Honor have any
8 more questions about Mr. Beaton's approach?

9 THE COURT: Yeah. One of the other things that
10 struck me is he made a distinction between kind of general
11 economic obsolescence and specific economic obsolescence and he
12 said that they were two different things. I'm trying to find
13 your chart where you have the definition. If you look at the
14 definition of the general deductions, which is your tab 2 in
15 your demonstrative exhibits, general obsolescence includes
16 things like competition and the costs or the increased cost of
17 raw materials, doesn't it?

18 MR. QURESHI: I'm sorry, Your Honor I'm just trying
19 to find the --

20 THE COURT: It's your tab 2.

21 MR. QURESHI: Okay. Your Honor, the general
22 obsolescence factors -- recall that those deductions were
23 arrived at by Mr. Beaton through his application of --

24 THE COURT: I understand that. And they include,
25 though, among other things, competition and the cost of raw

1 materials, don't they?

2 MR. QURESHI: Your Honor, only on a general basis.

3 THE COURT: Okay. Then if you look at his specific
4 economic deductions, which are tab 3, they also include the
5 high cost of raw materials. And when I see things like
6 globalization, I think of competition. So what are the
7 differences between the two?

8 MR. QURESHI: Your Honor, I think that the
9 fundamental difference is this: that the first category is a
10 general deduction. Those just assume that it's this machinery
11 anywhere in the United States in any industry in the United
12 States. It's not specific to --

13 THE COURT: I understand that's what he testified to.
14 But what's the difference, say, between the general increase in
15 raw materials and the specific increase that he assumed?

16 MR. QURESHI: I think the difference, Your Honor, is
17 that when he talked about, under the general category, this
18 piece of equipment being located in no particular place --

19 THE COURT: Right.

20 MR. QURESHI: -- in the United States and in no
21 particular market condition in the United States. I think
22 there would be general inflationary pressures that would cause
23 some raw material increase. And then you look at the specific
24 which is here's the plant in Palmetto. Here are the supply
25 contracts for raw materials for this plant in Palmetto. Here's

1 the fact that seventy percent of those contracts don't have raw
2 materials pass-through provisions in them, raw material price
3 increase provisions there. That gets to the specifics.

4 THE COURT: Well, why am I considering things
5 specific to Wellman if I'm trying to figure out what a
6 hypothetical buyer would pay for these assets?

7 MR. QURESHI: Because, Your Honor, the hypothetical
8 buyer is going to buy these assets where they're presently
9 located and operating in the manner that they are presently
10 operating. We're not assuming that the hypothetical buyer here
11 is going to take the plant at Palmetto and move it to
12 Louisiana. We're assuming that the hypothetical buyer is going
13 to step into that plant, as it is today, and operate that
14 plant. And so, one therefore needs to analyze these specific
15 obsolescence factors that affect that plant where it's located
16 and the manner in which it is presently operating.

17 Your Honor, again, unless there's more questions on
18 Mr. Beaton, I think I'll move on to --

19 THE COURT: Okay.

20 MR. QURESHI: -- the comments about Mr. Lerman's
21 approach. And, Your Honor, I said in my opening statement that
22 the cross-examination of Mr. Lerman would show that his
23 methodology is fundamentally unreliable. And I think, Your
24 Honor, that it did -- to the point that I would submit, Your
25 Honor, there is no value left from the first liens that Your

1 Honor could have, with any support, rely on. And it's a long
2 list. I don't want to belabor it. And, frankly, I don't know
3 where to begin. I'll start with the DCF because the DCF
4 approach is, again, one that Mr. Lerman relied on the most,
5 said it was his best, his best value. Start with the fact that
6 it was twenty million dollars higher than his other approaches.
7 But even that aside, Your Honor, it was truly remarkable that
8 Mr. Lerman testified that he only knows of one way to calculate
9 a terminal value. Truly remarkable. His own textbook that he
10 cites in his report and every textbook that Your Honor could
11 possibly find on valuation tells you that there are two ways to
12 calculate the terminal value. And the terminal value here
13 accounts for a huge portion of his computed value. And those
14 textbooks all say either the perpetuity method, also known as
15 the Gordon Growth method, or the exit multiple method. Mr.
16 Lerman testified that he had never heard of the exit multiple
17 method. Well, why is that important? One of the treatises
18 that we impeached him with, which is from Professor Pratt, a
19 well-known expert in the valuation field, talks about how
20 typically both methods are calculated and both are analyzed as
21 a cross-check on one another. If the results are wildly
22 inconsistent, this is, again, a way to ensure that there's more
23 reliability to support --

24 THE COURT: Did Mr. Schmitt use both methods?

25 MR. QURESHI: Mr. Schmitt, I believe, did use both

1 methods.

2 THE COURT: Okay.

3 MR. QURESHI: And Mr. Lerman never even heard of it.

4 But more severely, and, Your Honor, I would direct you to the
5 last tab in the book of demonstratives and -- I don't know,
6 does Your Honor have a copy of Mr. Lerman's expert report
7 handy?

8 THE COURT: Yes, I do.

9 MR. QURESHI: So let's go to page 97, which we spent
10 a great deal of time on, and -- actually, a couple of related
11 points that he made from looking at this one page. So if Your
12 Honor takes 2012 as an example, on page 97, we're looking at
13 the depreciation line and then the deduction for capital
14 expenses, the first that Your Honor will notice is that it's
15 almost all of the after-tax net cash flow is generated as a
16 depreciation expense. That, in fact, I believe that for 2012
17 it's more than a hundred percent that comes from depreciation.

18 THE COURT: But isn't it a wash? He's taking a large
19 depreciation expense as a deduction to reduce the net income
20 and then he's just adding it back.

21 MR. QURESHI: Your Honor, I --

22 THE COURT: It's essen -- putting aside the tax
23 ramifications, it's just a wash, isn't it?

24 MR. QURESHI: I don't think it's a wash because of
25 the way he applies his DCF here. He takes, through the

1 application of such large depreciation numbers, he generates a
2 very large after-tax net cash flow.

3 THE COURT: I'm saying, if he had a smaller
4 depreciation, he'd have a higher net income by the same amount,
5 though, wouldn't he?

6 MR. QURESHI: If he had a smaller --

7 THE COURT: In other words, if taking ten million
8 instead of nineteen million, he'd have ten million dollars more
9 in net income before taxes.

10 MR. QURESHI: That is true, Your Honor.

11 THE COURT: What I'm saying is it's just a wash for
12 cash flow purposes, isn't it?

13 MR. QURESHI: I don't think it's a wash. In your
14 limited example, Your Honor, I think Your Honor is right.

15 THE COURT: It affects taxes but otherwise it's a
16 wash.

17 MR. QURESHI: If Your Honor looks at a single year, I
18 think that's right. It is a wash.

19 THE COURT: But every year he's adding back the same
20 amount of depreciation that he's deducted in computing the net
21 income. That's -- by definition, that happens every year.

22 MR. QURESHI: For each individual year, Your Honor, I
23 think that's right. But where it becomes a very severe error
24 in this analysis is because he takes those cash flows, he
25 assumes perpetuity growth rate, which, in this case, is three

1 percent. And this gets to the quote that is on the
2 demonstrative which is from his own book, Professor Hitchner.
3 And they characterize it as this, as a common mistake. It
4 doesn't make sense, Your Honor, to assume growth into
5 perpetuity when you've assumed such large depreciation numbers
6 that that asset is going to be gone in five years. That's the
7 only thing he did. That's his only methodology for calculating
8 his DCF. And his own textbook says not only that you shouldn't
9 do it but it calls that method a common mistake. And every
10 other textbook that Your Honor will find on valuation will tell
11 you that that is a fundamental misapplication of the Gordon
12 Growth method. Now, if Mr. Lerman had also calculated through
13 the application on an exit multiple, a terminal value, then
14 maybe there would be one leg for his DCF left to stand on. But
15 he didn't. That's all he did.

16 And so, Your Honor, because of that failing, I truly
17 believe that there's simply no basis to rely on his number.

18 Now, Mr. Lerman also characterized his assumption,
19 his projection, as conservative. And, again, Mr. Serino
20 touched on a couple of these and I won't belabor it. He used a
21 few examples in cross-examination. Natural gas prices,
22 electricity prices frozen back in 2007 bear no relationship to
23 the reality that are very significant given the high portion of
24 Wellman's costs that come from its energy expense.

25 Overhead. Mr. Lerman argues that the hypothetical

1 buyer here, because they're in the business, they're going to
2 have a CFO, they're going to have a CEO, they're going to have
3 a court restructure in place. And therefore, he assumes zero
4 overhead. He doesn't say --

5 THE COURT: Well, he said there would be additional
6 people at the plant.

7 MR. QURESHI: Absolutely. But he assumes zero costs
8 for -- and his DCF showed a zero on that line.

9 THE COURT: I thought that was added to the projected
10 labor expenses.

11 MR. QURESHI: I think Your Honor might be referring
12 to one of his analyses where he takes a deduction for certain
13 costs. But in his DCF model, he does not deduct from cash
14 flow, a line item for SG&A costs for overhead. Now --

15 THE COURT: Well, he has labor costs in here. I
16 mean, there are costs there that he deducts.

17 MR. QURESHI: And those costs, Your Honor, don't even
18 come close to what Wellman actually incurs. Your Honor,
19 Wellman's own forecast shows that Wellman incurs average --
20 average annual SG&A costs of thirty-five million dollars. Mr.
21 Lerman has, in his report, averaged EBITDA of sixty-one million
22 dollars. Now if he deducted from that EBITDA number the actual
23 overhead costs that Wellman incurs today, it's quite obvious
24 what the effect would be on his DCF.

25 THE COURT: But wasn't his point that a hypothetical

1 buyer will at least have some of these elements in place. When
2 J.P. Morgan took over Chase, you didn't have two CEOs, you
3 didn't have two CFOs. You probably didn't have two accounting
4 departments. You eliminated a lot of the overhead.

5 MR. QURESHI: Absolutely. And there absolutely would
6 be some synergies that would benefit the hypothetical
7 purchaser. And, Your Honor, I completely agree that there is
8 absolutely an argument to be made that the hypothetical buyer
9 here might not have SG&A costs as high as Wellman's. Wellman,
10 again, thirty-five million dollars a year -- the buyer might be
11 able to do it for less.

12 THE COURT: Well, how do you determine the
13 incremental costs of SG&A?

14 MR. QURESHI: I'm sorry?

15 THE COURT: How would one determine the incremental
16 costs of SG&A?

17 MR. QURESHI: Well, Your Honor, I'm certainly not an
18 appraisal expert so I couldn't walk Your Honor through every
19 step in that. But I will say this. Mr. Lerman was clear in
20 his testimony and his report that he takes no deduction for
21 this overhead. Now, he also agrees that the hypothetical buyer
22 will incur costs. They're going to have to run these plants.
23 They're going to have to have an infrastructure in place.

24 THE COURT: Well, I thought he testified that there
25 would be additional people at each of the plants.

1 MR. QURESHI: Well, Your Honor, in his DCF, I don't
2 see the line item deduction that one normally does --

3 THE COURT: Well, there's labor costs amongst the
4 expenses. And I thought he testified that that included --

5 MR. QURESHI: Your Honor, that's --

6 THE COURT: Let me finish. To the extent necessary,
7 an additional person or people at each of the plants. That
8 would be the incremental overhead.

9 MR. QURESHI: Your Honor -- if Your Honor's referring
10 on page 96 in his direct labor line item --

11 THE COURT: Well, it's a labor item. I don't whether
12 it's operating expense or salaries, but I do remember him
13 testifying to that.

14 MR. QURESHI: Well, certainly, I don't believe, Your
15 Honor, that any of these labor categories that he has listed as
16 fixed expenses at the plant level involved overhead costs at
17 the corporate level. They're all plant specific. And Your
18 Honor may also recall that Mr. Lerman testified --

19 THE COURT: Well, so what overhead at headquarters,
20 to distinguish from the plant, would a buyer have to incur that
21 it wasn't already incurring being in the business?

22 MR. QURESHI: Most significantly, SG&A, selling,
23 general and administrative expenses.

24 THE COURT: But like what if it's in the business
25 already? There are certain economies of scale, I would think.

1 MR. QURESHI: Absolutely, there are certain economies
2 of scale. Your Honor, they're going to have go out and find
3 customers. They may have customers for their existing product.
4 But, as Mr. Beaton explained, just like Wellman isn't going to
5 rely for all of its raw materials on a sole sort of supplier,
6 so, too, the customers, are not going to rely just on Wellman
7 for all of their products. So depending on what customers that
8 hypothetical buyer has and how much overlap there is with
9 Wellman's existing customers in a market where customers are
10 very concentrated and very few, there will be an expense
11 associated with that. But just generally, on the day to day
12 operation of the business, there's three new tenants. And
13 they're making millions and millions of pounds of this product
14 every year and that product has to be sold, that there are
15 accounts to be managed, there are raw material supply chains to
16 be managed. And all of those functions currently at Wellman
17 are in the corporate overhead number. That's what that thirty-
18 five million dollars --

19 THE COURT: But wouldn't a buyer -- I understand that
20 there's more work. I'm not arguing with you. But wouldn't a
21 buyer have a sales force and have a force to manage production
22 already?

23 MR. QURESHI: A buyer would have those things. But
24 to suggest that a buyer could take these three plants and all
25 of Wellman's production and at zero incremental cost go out and

1 operate the business? It's unrealistic to think --

2 THE COURT: I don't think that was what Mr. Lerman
3 testified to in the end. Because, as I said, he did identify
4 some additional labor costs.

5 MR. QURESHI: To the extent he did, I don't think
6 they come close to approximating the true --

7 THE COURT: Okay.

8 MR. QURESHI: -- costs that would be incurred by the
9 hypothetical buyer.

10 And, Your Honor, again, continuing with the theme of
11 can Mr. Lerman's report be relied upon and against their review
12 of the DCF, his discount rate, obviously a very critical piece
13 of his analysis -- virtually every valuation expert that I have
14 seen, Your Honor, calculates a specific company specific
15 discount rate applied to the company that that expert is
16 attempting to value and does it currently. His first approach,
17 Mr. Lerman's first report, took the 2007 Morgenstar yearbook
18 which had data only through March of 2007 and everything else
19 in that book is through 2006. He took that industry discount
20 rate and applied it to the full projection period of Wellman's
21 earnings, through 2012.

22 THE COURT: Well, assuming that was a starting point,
23 how should it have been modified in order to make it company
24 specific?

25 MR. QURESHI: Well, Your Honor, I would start with

1 page 5 of Morningstar, which is his source book. It says right
2 in here "it is our position that the models utilized in this
3 book provide cost of capital statistics will be useful when
4 applied on a uniform basis to the industry as a whole. On an
5 individual company basis, the models utilized in this book may
6 provide information that is inaccurate or misleading." That's
7 what he did. There are well recognized methodologies for
8 calculating the cost of capital for this specific company. Now
9 I don't know if Mr. Lerman just doesn't know how to do it.
10 There's a distinct possibility that that's the case given that
11 he doesn't know how to calculate an exit multiple. But he
12 didn't do that here. He just took an industry. And an old one
13 at that when the book tells him not to do it, his source book.
14 The same source book that, by the way -- I mean, he had no idea
15 even what companies were looked at in this source book to
16 arrive at that industry discount rate. He didn't know --

17 THE COURT: Was that the Morningstar book you're
18 talking --

19 MR. QURESHI: This is the Morningstar book. He
20 didn't know whether the comparable companies were included. I
21 asked him the question at his deposition, Your Honor, and he
22 said I'd have to phone Morningstar to find out. He didn't even
23 look in the appendix. It's right here. And so, one really has
24 to question whether Mr. Lerman, with all due respect, knows
25 what he's done. I don't think he does in the DCF. I think

1 it's fundamentally unreliable.

2 So, Your Honor, unless the Court has any other
3 questions, I think I will rest.

4 THE COURT: Thank you.

5 MR. QURESHI: Thank you.

6 MR. PARKINS: Your Honor, may I hand you some
7 demonstrative exhibits, please?

8 THE COURT: Sure. Thank you.

9 MR. PARKINS: Page 43. Your Honor, before I get into
10 my prepared argument, I just want to answer a couple of your
11 questions, if I may.

12 THE COURT: Sure.

13 MR. PARKINS: If we look, Your Honor, at page 75 of
14 volume 3 of the Schmitt report --

15 THE COURT: This is Mr. Schmitt's report.

16 MR. QURESHI: -- in the Business Enterprise Valuation
17 section, Your Honor --

18 THE COURT: 75?

19 MR. PARKINS: Yes, Judge.

20 THE COURT: Okay. If you go down to the last
21 paragraph on the page there, Mr. Schmitt says he used the
22 Gordon constant profile.

23 THE COURT: Um-humm.

24 MR. PARKINS: You asked the question what he used and
25 counsel said he used both. That wouldn't be true. He used the

1 Gordon cost approach model.

2 THE COURT: I'm sorry.

3 MR. PARKINS: I'm sorry?

4 THE COURT: What does that refer to?

5 MR. PARKINS: The growth model for calculating the
6 terminal year. You asked what Mr. Schmitt did and I think
7 counsel he did both. And Mr. Schmitt did one on the same one
8 that Mr. Lerman did.

9 On the second point, Your Honor, with respect to
10 discount rates when Mr. Lerman got the new book from
11 Morningstar, he used discount rates that were higher than those
12 he used by Mr. Schmitt, which is reflected two paragraphs up,
13 Your Honor, which means --

14 THE COURT: So how come he wound up with such a
15 higher number?

16 MR. PARKINS: Well, I'm going to get to that.

17 THE COURT: Okay.

18 MR. PARKINS: I'm going to get to that. Your Honor,
19 one of the questions you asked earlier today was should you be
20 concerned about the fact that the liquidation value in the
21 debtors' disclosure statement was 65.8 million dollars and Mr.
22 Schmitt's number was 70.8 million dollars and Mr. Beaton's
23 number was seventy-four million dollars. Well, before I really
24 get into the nuts and bolts of what I'm going to talk about,
25 I'd like to remind you that on direct examination when Mr.

1 Schmitt testified about a check he did on his seventy million
2 dollar number, he said well, seventy-nine or seventy, within
3 the range, they're the same basically. I think you can recall
4 that testimony. So what we have here is the numbers by the
5 seconds and the company being in the range of liquidation.
6 This is what it is. It's the same numbers.

7 But let me, if I may, Your Honor, really get to the
8 heart of some of the issues here and I'd like to talk about
9 some of the other numbers which I think you should be concerned
10 about with respect to Mr. Schmitt's report. And if you'd look
11 with me, Your Honor, at the tab number 1 and tab number 5 --
12 I'm sorry, tab number 6. I'm sorry, I'm wrong. I was right.
13 Tab number 5 and tab number 1, one of the fundamental issues
14 that we chased during the entire hearing, Your Honor, if I may,
15 was the enterprise value. There's a 273 million dollar
16 enterprise value which appeared on counsel's same page 43.
17 That's this figure number here, this 273 million dollar number.
18 Interestingly enough, Your Honor, what we have here is that Mr.
19 Schmitt's number of 273 million dollars was presented in his
20 expert report on July 3rd. On July 25, and then for a hearing
21 set the day before the valuation hearing was set, the debtor
22 filed a supplemental disclosure statement and disclosures --

23 THE COURT: Hold on for a minute. Can everybody hold
24 it down so I can Mr. Parkins? Go ahead.

25 MR. PARKINS: Supplemental disclosure statement and

1 supplemental disclosures. And if you look with me at Exhibit
2 number 5, Your Honor, it's the valuation analysis, which is
3 Exhibit D to the disclosure statement, which Your Honor found
4 had contained adequate information. What you have here is the
5 fact that Lazard, the debtors' investment --

6 THE COURT: By the way, my copy has yellow
7 highlighting.

8 MR. PARKINS: Yes. I did.

9 THE COURT: I assume that the other copies -- okay.

10 MR. PARKINS: Everyone has yellow highlights. The
11 colors, the highlighting, is shared everywhere, Your Honor.

12 THE COURT: Okay.

13 MR. PARKINS: Shows that the Lazard get an enterprise
14 valuation and Lazard's midpoint of its enterprise valuation is
15 337 million not an enterprise valuation of 273 million. Now,
16 Lazard had this 273 million dollar number for three weeks
17 before it presented its enterprise valuation to the Court in
18 its disclosure statement for the debtor and it rejected the 273
19 million dollar number --

20 THE COURT: Why didn't you ask Mr. Yearley about that
21 on cross-examination?

22 MR. PARKINS: He didn't bring it up. I was waiting
23 for this. I didn't bring it up, Your Honor, because I didn't
24 want to affect the numbers that are already in the disclosure
25 statement. I didn't want to ask him questions.

1 THE COURT: Okay.

2 MR. PARKINS: This is his numbers. But this is in
3 evidence.

4 THE COURT: Correct.

5 MR. PARKINS: This is BNY number 1. So what we have
6 here is the debtors' statement that the enterprise value, and
7 it uses this term "enterprise value" of the debtor as of
8 September 30, the same date that Mr. Schmitt picked is 337
9 million dollars. So what I'm going to ask before I go up to
10 the board and say are these apples to apples comparisons, I
11 ask, Your Honor, maybe not today but in consideration of
12 whether these are apples to apples comparisons to determine
13 whether or not the effect of what I'm going to say here is
14 true, is look with me at the beginning of page 74 of the
15 Schmitt report.

16 THE COURT: Which volume?

17 MR. PARKINS: It was the page we looked at before.
18 It's volume 3, Judge, page 74. And if you look there, his
19 business enterprise valuation where he tried to determine the
20 enterprise valuation and he goes through the discounted cash
21 flow methodology, guideline publicly traded methodology,
22 etcetera, to reach his 273 million dollar number. When you
23 read the discussion by Lazard, and if you turn the page to the
24 second page of this tab 5, and you look at the second full
25 paragraph there -- the first full paragraph that begins

1 "Hypothetical evaluation estimates", you will see that Lazard
2 did the same thing as Mr. Schmitt did. But Lazard had Mr.
3 Schmitt's enterprise valuation for three weeks and rejected it.
4 And we submit, Your Honor, that you should, too, because what
5 this does, what this does when you use Lazard's midpoint, Your
6 Honor, is if you put Lazard's number here for -- the
7 methodology he used is deduct, deduct, deduct. If you put
8 Lazard's number -- the debtor is an investment banker. He
9 knows it's going to be for nine months not someone hired to
10 just do the project. If you put here 337, you get down to not
11 our number, seventy million, you get down to a number 134
12 million if you use Lazard's enterprise value. And I submit,
13 Your Honor, if you study these, the valuations and Mr.
14 Schmitt's valuations as to getting to his enterprise value,
15 you'll see that the methodology is the same but the company
16 that really knew this company, then considered these
17 opportunities, knew and concluded that the midpoint of the
18 valuation of the enterprise value was 337 million dollars.

19 What that does, Your Honor, is it said we have chased
20 because no one checked before Mr. Schmitt put his evidence on
21 the record that there is possibly a difference between the two
22 experts for the debtor, Lazard and Mr. Schmitt, the enterprise
23 valuation was approximately 60,000 dollars higher. That's
24 60,000 dollars and there's immediately on the record for my
25 client, Bank of New York. And I say if you're troubled, as we

65

1 were troubled, by looking at these numbers which are in
2 evidence, you should be troubled by the fact that the Lazard
3 enterprise valuation that everyone relies on here for the case
4 for the debtor busts Mr. Schmitt's numbers by sixty million
5 dollars, all of which are generous to Bank of New York.

6 Now, if you go back with me to tab 1, Your Honor, of
7 my handout, tab 1 reflects in yellow here, we tried to build
8 this, page 1 of 4 going through page 4 of 4, sort of
9 incremental growth of the evidence as presented in the various
10 documents and testimony.

11 If you look at page 1, you see BNY Number 1 of
12 Exhibit D, the number we just went through, the 337 million
13 dollar number in evidence, debtor's PP&E book value of 630, 237
14 million. These are all annotated for Your Honor to go and
15 verify where these came from. You have the PP&E valuation,
16 which is what I just did here, which is what Mr. Schmitt takes
17 to determine the seventy million dollars to validate that every
18 scenario that he went with, Mr. Chase's seventy million dollar
19 number, this number was wrong because it was our identified
20 valuation. It's sixty million dollars higher.

21 And then you have the debtor's, Lazard's, PP&E
22 liquidation value of 6/30/08, of 65.8 million dollars, which we
23 talked about.

24 One thing I would like to point out, Judge, when you
25 study the Lazard analysis of value and Mr. Schmitt's, they're

1 both done as of September 30. So they're apples-to-apples date
2 using the same methodology.

3 If we go to page 2 of 4, Judge, we add the increment
4 of the Grant Thornton and the AccuVal valuation, and they're in
5 the red there. And they're added as increments here for the
6 Court to see as we build upon this to see where the numbers
7 actually fall out.

8 If we go to page 3 of 4, we see the Lerman numbers.
9 And you'll see the Lerman numbers, the high value of 197, 181
10 and 136. Amazingly, when you use the appropriate enterprise
11 value that was argued determined as the right enterprise value,
12 we see the two valuations of the raw PP&E coming together, the
13 lowest numbers, the minimum, between the correct calculation
14 using Lazard's identified value with Mr. Lerman's low number
15 calculation. They come together. They are a subtraction of
16 the working capital. They are a subtraction of the enterprise
17 value. They come together in the same numbers. Interesting.
18 Not a coincidence, Your Honor.

19 And then, as you turn the page, Your Honor, what we
20 did in here is we took those existing numbers and we put in
21 purple here what we believe is the overzealous penalizing done
22 by AccuVal and Grant Thornton, much of which you questioned
23 about here. And we deducted, for example, from AccuVal, the
24 103 million dollar -- this number here, unquantifiable,
25 undefinable 103 million dollar number. You can't quantify it.

1 You have plenty of line items. We took that out.

2 And then with respect to Mr. Beaton and Grant
3 Thornton, we took out one of his double hits. Instead of
4 making it seventy-five percent, or seventy-five million
5 dollars, we said since there's no quantification, what if it
6 was only half? And the numbers show up here.

7 So what you see at the end of 4 of 4 here is sort of
8 the aggregation of the numbers. The purple ones are the ones
9 we think are erroneous and overstate the penalties that both
10 Mr. Schmitt and Grant Thornton have put in their numbers. But
11 the rest are actually numbers that are in evidence with Your
12 Honor, are calculated from the correct Lazard enterprise value.

13 Now, if you go, Your Honor, with me to tab number 2,
14 I think tab number 2 and tab number 4, tab number 2 is a time
15 line we put together. And you can see it's annotated for the
16 evidentiary documents which support where we got this time
17 line.

18 What's important about this, Your Honor, is a couple
19 things. Number one, what it shows is that when Lazard started
20 its effort to try to market the companies back in November of
21 last year, Your Honor, the EBITDA projections for '08 and '09
22 are eighty-three and eighty-nine million dollars. If you turn
23 with me, Your Honor, to tab number 4, you'll see that by
24 February, indications of interest had been generated from three
25 bidders. And based on these numbers, these are the only

1 numbers that were presented to these people, as testified,
2 okay? You see that the offers that were being discussed -- not
3 offers. I'll call them indication of interest because there
4 were no bids. The indications of interest, at this time with
5 the EBITDA numbers presented by the company, Your Honor, were
6 400 million dollars or higher with cash.

7 Now, what happened after this date? Go back to my
8 time line. After this date, the company filed bankruptcy.
9 This is tab number 2. The company filed bankruptcy, and the
10 DIP budget showed an EBITDA projection of thirty-five. We all
11 sat here on the first day of court and we know what the lender
12 said had to be done and where to get DIP financing. They said
13 you had to go sell. Let's not kid ourselves. We had to sell.
14 I remember Your Honor ruling there was no choice and had to go
15 sell. There wasn't a reorganization alternative.

16 I remember you arguing that the debtor should have
17 the leeway to use the tools of bankruptcy, and the lender said
18 no. So they had to go sell. What happened is offers came in,
19 and sure enough, offers came in with lower EBITDA numbers of
20 250, 260 million dollars.

21 But, voila, what happened now, Your Honor? What
22 happened now is that in May, the debtors projections for 2009
23 and 2010 come out, and those numbers appear in evidence.
24 They're Exhibit Number 22, which I think is tab 7 in this
25 booklet here. The EBITDA numbers go up. The EBITDA numbers go

1 up projected for '09 of sixty-nine million dollars and
2 projected for '10 -- I think it's seventy-four million dollars.

3 And, Your Honor, it is no coincidence when the EBITDA
4 numbers go up the Lazard's enterprise value is 337 million
5 dollar midpoint. Shocking, isn't it? No wonder the offers of
6 250 million dollars were not accepted. No wonder they were too
7 low. It is not shocking that we have a 337 million dollar
8 enterprise value and don't accept an offer that's 90 million
9 dollars less. Why would you? And it's also, Your Honor, clear
10 that the sales efforts stopped when these numbers became
11 published.

12 So what we have here, Your Honor, is at the same time
13 that the EBITDA numbers go up and the enterprise value goes to
14 337 million dollars, clearly sort of approaching the 400
15 million dollar number, but if you start back in October, these
16 numbers were an EBITDA of eighty-five. Eighty-five million
17 dollars, eighty-three million dollars and ninety-million
18 dollars less than the four hundred million dollar cash offers
19 but approaching them again because EBITDAs are going up.

20 At the same time, you have the AccuVal report. At
21 the same time the new EBITDA numbers come out, the AccuVal
22 report says the value of the PP&E is seventy. Well, Judge, we
23 have here the enterprise value of 337 and 870. It's 134
24 million dollars. Just not right. It doesn't fit.

25 THE COURT: But you've been talking about the Lazard

1 valuation. What about the Lerman val?

2 MR. PARKINS: The difference between Lerman's
3 valuations and the numbers we've been talking about are
4 threefold. Number one, Lerman did valuations of the plants.
5 Lerman did not do valuations of the company. Lerman was given
6 information with regard to the plants' P&Ls, the plant costs,
7 the plant equipment, plant margins, etcetera.

8 So, Lerman, as he said on the stand, said this is an
9 asset play. Questions raised by counsel for the second lien
10 holders that SG&A is not included, it would depress the cash
11 flows, of course wouldn't be included for the same reasons Your
12 Honor asked the questions. If I have a big sales force or
13 buying force, having one more or two more plants is not going
14 to require me to incur dramatic SG&A. In fact, it probably
15 wouldn't be anyway because the customers in the universe are
16 identified, and the suppliers in the universe are also
17 identified.

18 THE COURT: Getting back to Mr. Lerman --

19 MR. PARKINS: Yes.

20 THE COURT: -- I recall him saying at least ten
21 times, when asked a question on cross-examination, well, I
22 didn't have the information, the debtor didn't give it to me.

23 MR. PARKINS: Right.

24 THE COURT: I'm not blaming him for that but doesn't
25 that undercut the probative value of his report? If he didn't

1 have the information that he apparently thought he needed to do
2 the valuation --

3 MR. PARKINS: It undercuts probative value if you
4 believe that the corporate overhead and corporate numbers,
5 okay, would be probative of the value of the plants. It
6 doesn't undercut necessarily -- what it did is he couldn't
7 validate the corporate numbers with respect to going out the
8 years with respect to the depreciation, but it doesn't undercut
9 the fundamental numbers with respect to the productive and
10 earning capacity of the plants. That didn't change whatsoever.

11 What he didn't have is numbers to validate how the
12 company was going to take, I think he said, depreciation,
13 didn't have whether or not they were going to use the, for
14 taxable purposes, use the book value or some other value for
15 determining depreciation. Didn't have that, and that's where
16 the numbers come ajar.

17 But the fundamental economics of the plan do not come
18 ajar, and he was valuing the fundamental economics of the
19 plant.

20 THE COURT: Well, he also assumed, I think, the same
21 useful life, the equipment that Palmetto and Pearl River --

22 MR. PARKINS: Correct.

23 THE COURT: -- and I forget, one was only nine years
24 old and one was -- some of the equipment was as much as
25 thirty --

1 MR. PARKINS: Ten years old.

2 THE COURT: Well, some of the equipment was as much
3 as thirty-five years old --

4 MR. PARKINS: Correct.

5 THE COURT: -- in the other plant. Yet, he assumed
6 that, in both cases, the useful life would be thirty-five
7 years.

8 MR. PARKINS: Correct.

9 THE COURT: Isn't there a sort of a disconnect there?

10 MR. PARKINS: No. Not really. The issue of
11 maintaining these -- these plants had fifty, sixty year lives.
12 As he said, one refinery is a hundred years old and continues
13 to operate full throttle.

14 THE COURT: Well, wouldn't the plant with the newer
15 equipment have a longer useful life, then?

16 MR. PARKINS: A plant with newer equipment will have
17 more efficient life. A plant with older equipment maintained
18 will continue to, as Mr. Lerman said, continue to perform at
19 capacity. In fact, Mr. Schmitt -- under cross-examination, I
20 asked him do you have any reason to believe these plants, as
21 maintained, with all the spare parts that exist, would not be
22 able to produce at full capacity? And the answer is no.
23 There's no reason to believe they wouldn't be able to operate
24 at full capacity. And there's no reason to believe that these
25 plants would not be able to continue to have a useful life so

1 long as there's demand. Plants continue to operate in
2 perpetuity until they're shut down because there's no demand
3 for them. They are gigantic capital expenditures. Refineries
4 are very expensive, and they perform until their demand is no
5 longer necessary.

6 So I think, in his experience, which he brings
7 industry experience to the table, not appraisal experience,
8 industry experience, companies use these plants until the
9 demand stops. They have a useful life. They do have a useful
10 life that goes on and on. And there's no doubt. And his
11 example was you see a refinery was a hundred years old, I
12 think. It continues to perform full-blown today. Depreciated
13 probably to zero, I would surmise, but it continues to perform
14 fully today because there's demand.

15 THE COURT: Part of the evidence is also that he
16 assumed, apparently wrongly, that the debtor could pass along
17 all the increases in raw material cost. How does that affect
18 his analysis?

19 MR. PARKINS: I have an answer to that question.

20 THE COURT: Okay.

21 MR. PARKINS: The answer to that question, Your
22 Honor, is in tab number 7, and I've highlighted the pages. I
23 think it's page 6, page 10 and 11. This is information that
24 Mr. Lerman was given, but this is borne out by the projections
25 provided by the debtor.

1 You recall the big issue that's been raised here is
2 that these raw material costs can't be passed on and that, in
3 fact, there will be a squeeze on margins. Remember? There'll
4 be a squeeze on the margins --

5 THE COURT: Um-hum.

6 MR. PARKINS: -- because it can't be passed on.
7 Well, as we look at the debtor's numbers and the debtor's
8 assumptions in its business plan, Your Honor, you have to look
9 prospectively, not just historically. And I think Mr. Beaton
10 said historically there hasn't been any -- the margins have
11 constricted. Mr. Lerman agreed. But what do you have in the
12 projections of the debtors? You have projections of the
13 debtors of cost at raw margins, not squeezed raw margins. Raw
14 material cost assumptions were based on estimates of April
15 2008, future cost assumptions based on five percent increase.

16 And then if you go with me, Judge, to pages 10 and
17 11, from the debtor's own projections, and you look beginning
18 in year 9, 10 and 11, for example, gross profit percent margin,
19 you take select income statement, items go down. That's sales
20 gross profit percent margin, Your Honor. See it with me?

21 THE COURT: Which -- well, there are a lot of --

22 MR. PARKINS: The first yellow line.

23 THE COURT: The gross profit percentage margin?

24 MR. PARKINS: Right. The gross profit margin. Those
25 profit margins are constant, which means, contrary to what Mr.

1 Beaton testified, contrary to, quote, "the economic
2 obsolescence" that people testified to, the company doesn't
3 believe there's any economic obsolescence and its margins
4 collapsing over the next years. And, therefore, using their
5 own projections, which Lazard relied on, which the company is
6 putting forward in support of its plan of reorganization, it
7 would be an error to say that there's constriction of the
8 margins, and these costs couldn't be passed through because the
9 company doesn't show any penalty here. None.

10 So Mr. Lerman did accurate -- to argue otherwise may
11 be history but it's not tomorrow. It would be incorrect. So
12 the answer is in the company's own numbers and the assumptions
13 that were given.

14 Let me talk about one other thing that you talk
15 about, these huge numbers of functional obsolescence that were
16 put in as penalties. As penalties. Mr. Lerman, if you recall,
17 testified that yes, there's depreciation for age, which he
18 took. And I think it's in his report. I think. Let me find
19 it here. Depreciation for age and depreciation for what he
20 called functional obsolescence, physical deterioration and
21 functional obsolescence, which he discussed.

22 But being an engineer rather than being not an
23 engineer going in to appraise this, he went and peeled the
24 onion back. If you recall his testimony, he said to the
25 Wellman people what is the obsolescence you're going to suffer

1 in your equipment today versus the new equipment? And what it
2 was, Your Honor, was the cost of power of the cooling system,
3 the heating system he talked about, which he said Wellman said
4 was one cent per pound of product. Rather than saying there is
5 a universal functional obsolescence, he said what is it, how do
6 I measure that? And he measured it and he came out with
7 functional obsolescence numbers, very high deductions of cost.
8 Here it's table 15 in his report, Your Honor.

9 THE COURT: What page?

10 MR. PARKINS: It's on page 40, Judge. Rather than
11 just do -- I'm sorry. You have it?

12 THE COURT: Is this the --

13 MR. PARKINS: Yes.

14 THE COURT: You're talking about the Huron report?

15 MR. PARKINS: Correct.

16 THE COURT: Okay.

17 MR. PARKINS: Pearl River and Palmetto. What he did
18 is he took physical deterioration because they're old, okay?
19 And then he had functional obsolescence, twenty percent. What
20 is that number? That number reflects the cost per pound of the
21 difference in energy cost, which he asked Wellman, he's
22 testified, was the functional obsolescence they saw. Rather
23 than a broad spectrum antibiotic number without support, he
24 went and peeled the onion back and said what's the cost
25 negative going to be to burden this company? And these were

1 put into his calculus.

2 Now, let's talk about some more things about, if I
3 could, Your Honor, talk about more things about Mr. Schmitt,
4 that the fundamental underpinnings of Mr. Schmitt's
5 calculation, the enterprise value of Lazard, underpins and
6 undercuts his entire calculus, chasing the seventy million
7 dollar number.

8 Now, one of the things you asked about, and one of
9 the things we never got an answer for, if I can just here
10 approach, is before using Lazard's numbers, just using his
11 numbers, where did he get this 103 million dollar number?
12 That's an enormous number. You pointed out where did he get
13 it? The answer is if you use the 337, it would be 60 million
14 dollars less if you try to plug it into the other numbers he
15 used. But the answer is it's a plugged number. It's the
16 amount you have to get to in order to support the seventy
17 million dollar number, which he reached from various
18 methodologies.

19 One of the methodologies he used, for example, and I
20 ask you to turn to the last tab, Your Honor, to try to validate
21 his numbers, interestingly enough, I think tab 9, Exhibit 13,
22 the merger and acquisition method. It's the second page of
23 that tab, yes.

24 THE COURT: Okay.

25 MR. PARKINS: If you look at Exhibit 13, the merger

1 and acquisition method, Your Honor, if you recall, this is Mr.
2 Schmitt's comps, so to speak, for M&A, which he generated a
3 selected multiple for. And what was the one he gave the most
4 reliance to, the most weight to? Number 7, the Reliance
5 Industries USA transaction/purchase of this old, closed,
6 shuttered fiber plant, okay, which he gave the most comparable
7 to because, Your Honor, what he is assuming for the purposes of
8 valuing the Wellman facility is an idled shut plant. That's
9 why he gave the most weight to it.

10 Interestingly enough, Grant Thornton rejected this as
11 a comparable saying this is a liquidation on the ground. Mr.
12 Lerman rejected it as this is a liquidation on the ground. Mr.
13 Schmitt relied on it most, in error. And from that error, what
14 he did is he selected multiples for capacity and, in his other
15 valuation methodologies, took the low end as every multiple, as
16 you recall, the low end of every multiple for his Guideline
17 Public Companies' EBITDA, revenue, and not only the low end of
18 his multiple but below the chart to try to drive the values
19 down to achieve the seventy million dollars, which was his
20 effort to try to strip the going-concern value out of the PP&E.

21 But he always comes back to how do I validate this?
22 And I validate this by my business enterprise value, being
23 seventy, targeting seventy throughout his calculus. Well, that
24 enterprise value is wrong, and that number was 133 million
25 dollars.

1 Now, let's talk about Grant Thornton for just a few
2 minutes. What Grant Thornton did, Mr. Beaton did is as
3 follows: He assumed it would be a lights-out scenario. No
4 doubt about it. He said yes. And why is it a lights-out
5 scenario? Because he valued, instead of going concern, as Mr.
6 Schmitt tried to do, this kind of calculus using -- is the
7 wrong number but now the number, we know, is 337 million
8 dollars? Mr. Beaton didn't do that. He tried to build it from
9 the bottom up.

10 Now, what did he do? He went and priced 6,500 parts.
11 Six thousand five hundred parts. He didn't price a plant. He
12 went, and what we have is a catalog. If you went through the,
13 quote, "reams" of paper he said he didn't bring to court, what
14 we have is the catalog of used parts of Wellman with a price on
15 them. That's what we have as a starting point.

16 And he puts that data into the Marshall Valuation
17 Service Software, and that Marshall Valuation Software
18 automatically, as Your Honor picked up, takes a deduction for
19 economic obsolescence and takes a deduction for physical and
20 functional obsolescence, the physical and functional
21 obsolescence for Palmetto. And if you have the Grant Thornton
22 report with you, just going to page 35 of that -- I have an
23 extra copy here if you want.

24 THE COURT: I have it.

25 MR. PARKINS: You have it? Okay. If you just go to

1 page 35, Judge, and that's the example that was used in his, I
2 think, direct examination, what you see here is the first input
3 in his testimony was that, using the Marshall Valuation
4 Service, you have a deduction of fifty-three percent and
5 twenty-five percent. And this was done -- do you see that?

6 THE COURT: Well, that's for the real property.

7 MR. PARKINS: Yeah, but they did this for the -- he
8 testified he did it for all the assets. And then what you
9 have -- he did it for everything, the 6,500 pieces of assets,
10 real property, personal property, put it in the Marshall
11 number, outcomes is -- what goes into a twenty-five percent
12 economic obsolescence versus, you asked, Your Honor, the
13 specific obsolescence? Nobody knows. Nobody knows what those
14 numbers are. It just comes out a number and it includes
15 twenty-five percent economic obsolescence. Nobody knows.

16 THE COURT: But you didn't put in any evidence
17 challenging the Marshall valuation method. Are you contending
18 that it's inaccurate?

19 MR. PARKINS: No, we didn't but he just testified
20 it's a software program used by appraisers. But still we don't
21 know the answer as to how much "double-dipping", so to speak,
22 there is in economic obsolescence, general or specific
23 obsolescence. We can get the exhibit.

24 THE COURT: Well, what does the evidence show about
25 that?

1 MR. PARKINS: Well, we can get to the specific
2 obsolescence for sure, okay. We can get to the specific
3 obsolescence, for example, if we look at counsel's tab number
4 3. We can go through them right now. And, Your Honor, this
5 economic specific obsolescence is a fifty percent number. If
6 you look at the machinery and equipment number on page 35, it
7 is a fifty-four million dollar deduct number, without any
8 justification. There was evidence that there was no economic
9 empirical calculus for this number in his judgment.

10 Well, let's look through these line items and see if
11 they're reasonable for a second. First one is historical
12 inability of PP&E to generate positive cash flow due to factors
13 such as Wellman's financial condition. We submit, Your Honor,
14 that Wellman's financial condition, other than being low-lying
15 fruit available to be plucked for a low price, has nothing to
16 do with a buyer in the marketplace and, therefore, it is not an
17 economic obsolescence factor. It makes you a target but not
18 economic obsolescence for the buyer.

19 Globalization: The buyers in this industry, Alpha,
20 M&G, others, are part of that globalization. They're not going
21 to look at that as an obsolescence. They are spending money
22 today building new capacity. The opportunity to get new
23 capacity is something they want to do. That ties into
24 oversupply. Mr. Lerman testified within the industry the
25 trends of how the chemical industry looks at the timing of

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1 expending more capital. At slow times, they know that there's
2 going to be a rebound, he testified. And therefore, they start
3 building plants. Why? Because it takes three years to get
4 them online. You know it's going to turn. They cycles are
5 going to turn. It's going to be coming back.

6 So the oversupply is not a negative for a buyer. The
7 oversupply is indicative of when, today, you're going to spend
8 more money, put more capacity in when that oversupply and that
9 curve meets demand going forward. And, in fact, as Mr. Lerman
10 testified and as the examples were shown by Mr. Schmitt and
11 others, a lot of money is going into new plants. It is not an
12 economic obsolescence factor to be considered.

13 High raw materials costs: We've dispensed with that.
14 The company shows no constriction in its margins. Now, we
15 don't know what the third party buyers' margins are but we do
16 believe -- I think it's a reasonable inference to draw that a
17 third buyer who's not in bankruptcy, who's doing better than
18 Wellman is not going to suffer constriction in its margins just
19 as Wellman was a weaker player.

20 And Wellman's projections are they're not suffering
21 constrictions in their gross profit margins. Why would you
22 assume that a stronger player in the marketplace would do it?

23 And the last one here, which is truly quite
24 interesting, personal property, an integral part of the real
25 property, relocation costs and logistics will be significant.

1 I still can't figure out what that means because these plants
2 aren't going anywhere. Why is there going to be an incremental
3 cost?

4 Reliance is building a plant near where the South
5 Carolina plant of Wellman is. The other plant, Pearl River,
6 the new plant, is on the Mississippi River, close to
7 transportation, close to sources of selling and buyers of
8 materials. There's no incremental cost going to be incurred
9 here with respect to that.

10 And, Your Honor, the other thing that's important is
11 that my partner, Mr. Flores, had Mr. Beaton, on cross-
12 examination -- it was interesting that during his deposition
13 testimony, I think you recall, we talked about the fact that
14 Mr. Beaton didn't distinguish between items that he called
15 selling a holding cost and economic obsolescence. He put them
16 in the same list and said they were. And his testimony at
17 trial was you're right, my report was wrong and my testimony is
18 wrong and I'm clearing it up today.

19 So when asked fresh, before preparation, in his
20 deposition what the difference was, he couldn't find any. Only
21 when he got to trial in his cross-examination and prepared for
22 trial did he draw a distinction.

23 But let's look at these that he drew here. Selling
24 and holding costs, tab number 4. Customer relationships:
25 Well, every expert testified that every player in the industry

1 who does PET resin has customer relationships. There are a
2 limited number of customers. Everybody knows it. Everybody
3 knocks on their to sell them product. That's the way it goes.

4 Supplier relationships: The supplier for raw
5 materials are limited. BP's the largest one. Others are in
6 the industry but everybody buys from the same supplier.

7 Intellectual property: What Mr. Schmitt testified
8 about since counsel says that Mr. Beaton didn't value
9 intellectual property --

10 THE COURT: But didn't Mr. Beaton testify that you
11 had to back out these costs simply because everybody in the
12 industry had these same assets and they weren't going to pay
13 for them.

14 MR. PARKINS: Mr. Beaton said that if I come into a
15 transaction as a buyer, I'm not going to pay you value for what
16 I already have.

17 THE COURT: Right.

18 MR. PARKINS: But, Your Honor, what I am going to buy
19 is the PP&E, and the PP&E, if you remember, is -- pyramid, is
20 the foundation of the business, is the PP&E.

21 And so what people are coming into buy is the
22 foundation of the business. And while they're not going to pay
23 for what they already have, they are going to pay for their
24 foundation. And usually you start the foundation first. But
25 they're coming in as a willing buyer and willing seller,

1 selling industry, who has, as I started out my first argument
2 opening day, the bundle of sticks, is going to be looking for a
3 PP&E plan.

4 One thing's for sure: It's not liquidation value.
5 One thing for sure, as you look at tab 1, it's not the
6 aggregation of the liquidation value. One thing we know for
7 sure is what Wellman thinks it is because of their enterprise
8 value. The calculus is 134 million dollars. That's the number
9 because no one challenges the deduction. Neither Wellman
10 didn't challenge, obviously, I'm not an expert, and the second
11 group challenged the deductive method here we're reaching the
12 replacement value of PP&E because this is what's left after you
13 deduct it from the enterprise value.

14 One thing I will add, Your Honor, is that in cross-
15 examination of Mr. Schmitt, when asked in his report and his
16 testimony what's the value of the intellectual property of
17 Wellman, he said very low. The testimony was very low. He put
18 twenty-eight million dollars for his value but the question is
19 not twenty-eight million dollars for the bucket of all the
20 patents and all the trademarks, as Mr. Lerman did. Again,
21 knowing what to do, peeled the onion back.

22 Mr. Lerman, in his assumptions, said what is a buyer?
23 Do I have to buy in order to put these plants into operation?
24 I don't have to buy the entire patent portfolio of Wellman. If
25 I needed to buy it, what I have to buy is the patents necessary

1 to put the plants in operation. And that is the number you see
2 in Lerman's exhibit, scenario number 3, of what I have to pay
3 to put these plants in operation. Not the entire patent
4 portfolio.

5 So what we have here, Your Honor, is the specific
6 cost that Mr. Lerman believed would have to be incurred,
7 including lost profits for sixty days of having to buy the
8 intellectual property, since I already had all the other bundle
9 of sticks, buy the intellectual property to put these plants in
10 operation.

11 And Your Honor asked one other question, I think, to
12 one of the counsel. Didn't, I think, you raise the issue of
13 wasn't it going to take sixty days to put the plants back in
14 operation? It was Mr. Lerman who used the Katrina example
15 because he testified when he was at the plant at Pearl River
16 that they were destroyed. It was down to bare bones, and they
17 put it back in sixty days.

18 He also used the example that he had personal
19 knowledge of an asphalt plant on the Gulf of Mexico that was
20 down, and it took them sixty days to reprogram their operations
21 and get back running full-steam.

22 So sixty days is a realistic number, as Mr. Lerman
23 testified. The crews work around the clock to get it up and
24 running. And, therefore, it is not a more protracted number.

25 Going back, Your Honor, and it's amazing because your

1 first question of the day was my last point of the day, and my
2 last point of the day in my tabs is tab number 8, which is your
3 questions on opening statements by Mr. Serino first day of the
4 hearing. And it was the question you started again with today:
5 Isn't it intuitively correct that the value of this plant is
6 worth more to someone who's going to operate the plant than
7 someone who's not?

8 The first question by the debtor and answer is,
9 "Difficult for me to say, Your Honor. It's difficult for me to
10 say." The Court, intuitively, "Doesn't that seem right?" Mr.
11 Serino, answer, "To -- it seems right but it's not right. It's
12 divorced from the standard of Rash. Rash said you don't think
13 about what the buyer is going to do with the business." Your
14 Honor, I submit that the definition of Rash and what a willing
15 buyer in the debtor's business trade or situation will pay a
16 willing seller is a fundamental part of what Rash mandates.
17 And the position of the debtor, trying to strip out what a
18 willing buyer brings to the table, what a willing buyer would
19 do with the business is a wrong interpretation of Rash. It was
20 the way that the debtor started out but said it didn't apply.
21 I submit, Your Honor, that when you look at tab number 1 and
22 you see the confluence, tab 4 of 4, and you see the confluence
23 of values provided in tab number 4 of the first tab, you will
24 see here, as I conclude, that the three bottom numbers here are
25 basically liquidation value. We have it. They can't escape

1 it. The debtor can't walk away from the fact that they've gone
2 in their disclosure statement, said these are liquidation
3 values.

4 And Mr. Schmitt testified that seventy and seventy-
5 nine are within the range. So this is all liquidation value.
6 You can't get away from it. When you put the correct Lazard
7 enterprise value in, the bottom numbers, the minimum numbers
8 for your own technology, PP&E, and Lazard's numbers are quite
9 close: 134.7 and Huron's 136.8. Very close because, Your
10 Honor, at the worst scenario taken by Mr. Lerman, the
11 deductions made here come out almost in tandem, the debtor's
12 number and Mr. Lerman's base number.

13 And one other thing that was testified about in Mr.
14 Lerman's direct examination, Your Honor, that he didn't use the
15 same growth factor. Your Honor caught it and said there's less
16 cash flow in Mr. Lerman's numbers for the first four years than
17 the other examples. That's true. Mr. Lerman tempered the
18 growth in his numbers, and therefore when you look at this
19 number here, Mr. Lerman's numbers are lower than what the
20 debtor's numbers would have generated under Mr. Lerman's
21 calculus, okay, but they run tandem to the debtor's numbers.

22 In conclusion, the motion of the debtor, Your Honor,
23 to value the PP&E at seventy must fail. It's a liquidation
24 value. The debtor's enterprise valuation numbers, based on new
25 EBITDA projections, based on what they've put in the disclosure

1 statement, what they're going after the creditors with, says
2 the midpoint of their enterprise value is 337 million dollars.
3 Even now, the math is 140 million dollars. The motion for
4 seventy must fail. Thank you.

5 THE COURT: Thank you.

6 MR. SERINO: Your Honor, may I have a brief rebuttal,
7 please?

8 THE COURT: Very brief.

9 MR. SERINO: Thanks.

10 THE COURT: Don't repeat anything he said.

11 MR. SERINO: Okay. Well, let me just address where
12 Mr. Parkins left off about the opening statements. He takes
13 them out of context a little bit because if you read the rest
14 of the opening statement --

15 THE COURT: What's the significance of the Lazard
16 valuation with a midpoint of 337?

17 MR. SERINO: Sure.

18 THE COURT: What should I do with that?

19 MR. SERINO: I think you should take it for what it's
20 worth. And what it is --

21 THE COURT: What do you think it's worth, the
22 disclosure in the disclosure statement?

23 MR. SERINO: Well, it's an apples-to-oranges-pears
24 comparison.

25 THE COURT: You talk a lot about fruit but --

1 MR. SERINO: Yeah. Well, let me think -- well, okay.

2 Let me tell you that Lazard did a going-concern valuation.

3 THE COURT: Well, it came up with an enterprise value
4 of 337.

5 MR. SERINO: Correct, on a going-concern basis.

6 THE COURT: Right.

7 MR. SERINO: All right? The other one we saw from
8 the disclosure statement --

9 THE COURT: Didn't -- well --

10 MR. SERINO: -- was the book value. No. That's what
11 I want to get to. This is not going concern. This is a
12 business enterprise value on a replacement value basis.

13 THE COURT: What did he do differently than you would
14 do if you did a going-concern valuation?

15 MR. SERINO: He did all the pieces separately and
16 built them up. He used the pyramid. He did not put them all
17 and say one plus one plus one is four.

18 THE COURT: I thought he did a discounted cash flow
19 analysis.

20 MR. SERINO: He did do a discounted cash flow
21 analysis, Your Honor, but he did it on a replacement value
22 basis. This is not a going concern. Here's the proof.

23 THE COURT: So what's the difference in the analysis?
24 That's what I'm asking you.

25 MR. SERINO: The difference in the analysis is the

1 Lazard number's a going concern.

2 THE COURT: Correct.

3 MR. SERINO: Okay. It includes assets that are
4 going-concern attributes, that the firsts don't have a lien on.

5 THE COURT: I understand that but isn't that 273
6 million number use the same methodology? It just comes out
7 with sixty million less.

8 MR. SERINO: No. No, because the 337 million dollar
9 number looks at the business as a whole.

10 THE COURT: Right.

11 MR. SERINO: Okay? It doesn't look at each piece --

12 THE COURT: Right.

13 MR. SERINO: -- and see what each piece is worth.
14 And when you take the business as a whole, there's some
15 synergistic effect. There's value to that, and going-concern
16 value.

17 Mr. Schmitt had to do something harder. He had to
18 look at each piece of the business on a replacement value
19 basis.

20 THE COURT: Yeah, but first -- but didn't --

21 MR. SERINO: All I have to sell is this.

22 THE COURT: -- but didn't he first value the business
23 and then subtract out the working capital and the intellectual
24 property, or the intangibles?

25 MR. SERINO: But even when he valued the business, he

1 did it on a replacement value basis.

2 THE COURT: What did he do differently than what
3 Lazard did? Or what did anybody doing a discounted cash flow
4 valuation do? That's all.

5 MR. SERINO: Your Honor, maybe here's a good example.
6 I'll try to show it, okay? I'm trying to say that what Mr.
7 Schmitt did was use the replacement value.

8 THE COURT: I understand what you're saying.

9 MR. SERINO: And I know --

10 THE COURT: I'm just asking what he did differently
11 than someone who's doing an enterprise valuation with it.

12 MR. SERINO: When he's building up, with his
13 replacement values, he came up with 173.

14 THE COURT: The buildup I understand --

15 MR. SERINO: Okay?

16 THE COURT: -- the bottom-up approach. But he also
17 did a top-down approach, and that's what that is, that 273
18 million dollar result.

19 MR. SERINO: He did a top-down approach --

20 THE COURT: Right.

21 MR. SERINO: -- and if you bear with me, hopefully
22 this will become clear.

23 THE COURT: Okay.

24 MR. SERINO: If this is his top-down --

25 THE COURT: Right.

1 MR. SERINO: -- 273, you take out 173, okay? You
2 have 273 replacement value business enterprise. You take out
3 173 replacement value working capital. Now, if you were going
4 to going concern, even Mr. Lerman tells you that the going-
5 concern value of the working capital is not 173, it's 195 if
6 you look at Mr. Lerman's report on page 34, okay? That's a
7 difference. It's almost --

8 THE COURT: And you're saying that that twenty
9 million dollar difference is attributable to what?

10 MR. SERINO: It's a going concern. It's a going
11 concern.

12 THE COURT: It sounds like he just used a different
13 number. Everybody used different numbers in those valuations.

14 MR. SERINO: Your Honor, what he basically did is
15 this: Mr. Schmitt had to figure out the replacement value of
16 the business. So the first thing he had to do was try to strip
17 away the going-concern additives to the business. That's this
18 outer shell. He strips away the going concern, okay? This is
19 Lazard's 337. It's the big building. It's the big circle.
20 Right there. Mr. Schmitt's 273 is inside. It's the business
21 enterprise value net of going concern. Mr. Schmitt builds that
22 up. Then he has a slice that's attributable to intellectual
23 property and tangible assets, a slice that's attributable to
24 working cap and a slice that's attributable to PP&E.

25 THE COURT: He didn't come up with that 195 million

1 dollar number through anything other than looking at Wellman's
2 historical balance sheet. And I'm looking at page 34. That's
3 where he got the number from.

4 MR. SERINO: You're talking about Mr. Lerman's
5 number?

6 THE COURT: Yeah.

7 MR. SERINO: Mr. Lerman's number --

8 THE COURT: It's a balance sheet number.

9 MR. SERINO: I think we're saying it is -- but it is
10 the going-concern value of the working capital.

11 THE COURT: You implied that the difference between
12 the 174 million, approximately, that Schmitt had for working
13 capital and the 195 or 196 million that Lerman had had
14 something to do with this going-concern concept. And all I see
15 is that Lerman picked his number off the balance sheet.

16 MR. SERINO: Your Honor, that is what I'm saying. I
17 guess what I'm trying to say is if you had to buy all three
18 elements of this business separately, use your analogy, there's
19 three stores. One store's the working capital store, and I go
20 and buy that. Another store's the intangible assets store, and
21 I go and buy that. And another store's the PP&E store and I
22 buy that. I'm going to pay a certain price for those three
23 pieces. I think, at the end of the day when I get all those
24 pieces together and I put them all together, I think it's going
25 to be worth more than the sum of my three costs. And I think

1 that's the difference between the 195 and the 173 here.

2 THE COURT: I don't see that.

3 MR. SERINO: I think that's the difference between
4 the 337 and the 273.

5 THE COURT: First of all, Lerman deducted a higher
6 number. So it should decrease. It works to Wellman's benefit
7 because it decreases the leftover that's going to be
8 attributable to property, plant and equipment.

9 MR. SERINO: But what Lerman did is when he went into
10 that store and he saw the PP&E, and instead of saying batteries
11 not included it said IP not included, intangible assets not
12 included, working capital not included. He didn't take that
13 into account. He didn't assume that the buyer with the bundle
14 of sticks is not going to go in that store and just take the
15 PP&E but pay for the working capital, the intellectual property
16 and the intangible assets.

17 THE COURT: Look, all I'm saying is he made a working
18 capital deduction the same way that Schmitt did that used
19 different numbers, but I don't see how anything has to do with
20 a long methodology of valuation. They picked different numbers
21 because they looked to different sources. That's all.

22 MR. SERINO: It is the wrong methodology, Your Honor.
23 Here's why.

24 THE COURT: You keep using that word "going concern",
25 and I just don't understand really the distinction you're

1 making.

2 MR. SERINO: The reason I use it is because of Rash.

3 THE COURT: I understand what Rash said. Okay. Go
4 ahead.

5 MR. SERINO: Let me try this example, Your Honor.

6 THE COURT: Go ahead.

7 MR. SERINO: Maybe this works. First, you got a car
8 rental business, and the firsts have a lien on one of those
9 cars.

10 THE COURT: Right.

11 MR. SERINO: That car has a Blue Book value of twenty
12 thousand bucks. Do we all agree that the replacement value of
13 that car is twenty thousand dollars?

14 THE COURT: Go ahead.

15 MR. SERINO: No. Let's say we didn't have that Blue
16 Book value. You had to figure out an income approach to the
17 valuation approach. And you look at the car rental price and
18 say it's a hundred dollars per day. There's 300 days in the
19 year. The income for the year is 30,000 dollars.

20 Now, that's an income approach that gives us a going-
21 concern valuation, something that is clearly more than the
22 replacement cost of that car. And the difference is --

23 THE COURT: Well, it may or not but --

24 MR. SERINO: It may or not --

25 THE COURT: -- but in your example, the car's an

1 income-earning asset, and there is information that you could
2 use to figure out what you could earn from it. It's not
3 necessarily true PP&E.

4 MR. SERINO: Well, I think PP&E is an income-earning
5 asset.

6 THE COURT: When combined with the other intangibles.

7 MR. SERINO: Well, that's the problem, though, Your
8 Honor. The firsts don't have a lien on those other
9 intangibles, and Rash says we have to value what they have a
10 lien on.

11 THE COURT: But they do have a lien on the increased
12 value of the PP&E because someone who's operating the business
13 would be willing to pay more for it?

14 MR. SERINO: No, Your Honor.

15 THE COURT: Okay, I --

16 MR. SERINO: No. You can't expect a buyer to come to
17 the table and pay the seller for something that the buyer
18 already has or that the buyer's not getting in the transaction.

19 THE COURT: So you think that someone who is
20 operating or is in the business --

21 MR. SERINO: Um-hum.

22 THE COURT: -- and wanted to buy this plant would pay
23 the same thing as somebody who's not in the business and wants
24 to buy the plant and just let it sit idle?

25 MR. SERINO: No. I don't think I agree with that,

1 Your Honor. I think --

2 THE COURT: Well --

3 MR. SERINO: I think it's worth more.

4 THE COURT: I would hope you wouldn't.

5 MR. SERINO: But I think the difference is -- the
6 difference could be as simple as replacement value versus
7 liquidation value. It may have a greater value. That plant
8 may have a greater value to someone who's going to use it than
9 someone who's going to liquidate it. But it doesn't mean that
10 that buyer is going to overpay for that plant and is going to
11 pay for things that they have on their own and that they're not
12 getting the transaction. It doesn't mean that when they walk
13 in that store, they're going to say well, I've got the working
14 capital, I've got the IP, I've got the intangible assets at
15 home, let me pay for it anyway. They're not going to do that.

16 And that's the fundamental difference between Lerman
17 and Schmitt. Lerman assumed that for one reason or another a
18 buyer's not going to be economically rational. A buyer's going
19 to come and say look, I got all the bundle of sticks, so I'm
20 going to pay you for that even though you're not giving that to
21 me, and that's going to boost up my PP&E value. That's what
22 Lerman assumes.

23 And, Your Honor, there's also just a couple of more
24 tic points. The remaining useful life discussion was
25 interesting. If this were actuarial tables, the position

1 counsel would be taking is that a nine-year girl has an
2 expected remaining life equal to a thirty-four old woman. It's
3 just not going to happen, right? And counsel says well, it's
4 very expensive, you can maintain plants for a hundred years,
5 it's very expensive. Well, try to do that on two million
6 dollars of capital expenditure. That's what Mr. Lerman asked
7 us to do.

8 We also saw, Your Honor, that they did what we
9 thought they would do. They attack the bids that came in in
10 March and April of 2008. They attack the fact that Wellman
11 didn't hit those bids, so to speak. But it's all it is, is an
12 attack. They had Mr. Yearley on the stand. He testified about
13 why those were real bids, about why Wellman never made a
14 decision whether he hit the bids or not. They could have asked
15 that question. They could have cross-examined him.

16 THE COURT: And he said it. It's in evidence. They
17 can refer to the valuation, the business valuation.

18 MR. SERINO: They can refer to the valuation, Your
19 Honor, but when you're comparing evidence, on the one hand,
20 with inference and insinuation, on the other hand --

21 THE COURT: It's evidence. That's what it says.
22 It's in evidence.

23 MR. SERINO: From what? Schmitt's report?

24 THE COURT: No. Well, Schmitt's report is in
25 evidence but the valuation that Lazard described for the

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1 enterprise.

2 MR. SERINO: No, no. I'm talking about the bids, the
3 230 to 260 million dollar bids that counsel wants us to
4 discount because he says well, those are distress bids, and
5 Wellman didn't hit those bids. The only evidence on that is
6 what Mr. Yearley said. They could have asked questions. They
7 chose not to. And that's the point there, Your Honor.

8 And another point, on Mr. Lerman's Exhibit 9, the DCF
9 model, I think I asked the wrong question. But Your Honor's
10 question --

11 THE COURT: Exhibit 9 that was given today or Exhibit
12 9 of his --

13 MR. SERINO: Oh, no. It's Exhibit 9 in his full
14 report. I think it's page 97.

15 THE COURT: Okay.

16 MR. SERINO: And something Your Honor asked today --
17 I'm sure you were talking to Mike and me, and that was you said
18 well, even if the depreciation goes down, you get what you
19 want, doesn't that just wash through the tax flow adjustment?
20 I think Your Honor is probably right there but our point, and I
21 didn't do a good job of asking, our point was this: Assume the
22 depreciation stays where it is but the capital expenditures go
23 up and meet or exceed the depreciation. On page 97. You've
24 got depreciation of 20.5 million dollars. See it on page 97,
25 Your Honor?

1 THE COURT: Right.

2 MR. SERINO: Depreciation of additional appreciation?

3 You've got capex of one million bucks. If the capex goes up to
4 meet depreciation by 19.5 million dollars, it wipes out his
5 adjusted after-tax cash flow of 19.1 million dollars in the
6 term of a year.

7 THE COURT: But there's no testimony that they're
8 going to spend twenty million dollars a year on capex.

9 MR. SERINO: There's no testimony that they're going
10 to be able to spend forty million dollars a year in
11 depreciation forever, and Mr. Pratt, the newsletter that Mr.
12 Qureshi put in from Mr. Pratt said in a three percent growth
13 model, you should assume that capital appreciation meets --
14 capital expenditures, rather, meet depreciation and exceed it
15 by fifteen percent. I'm saying forget the exceed by fifty --

16 THE COURT: All right. So if he's wrong in the
17 depreciation, the net income is higher and the depreciation --
18 the add-back to the depreciation is lower. That's all. What
19 difference does it make?

20 MR. SERINO: The difference it makes is, one, it
21 shows how implausible and how impossible his assumptions are,
22 where he can live in a world where you're going to depreciate
23 forty million dollars a year for perpetuity against capex of
24 two million dollars a year. And the proof is in the pudding
25 because you say well, let's say that's not reasonable, let's

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1 say it should be one-to-one. If it's one-to-one, this business
2 has no earnings. Then what happens to his valuation?

3 THE COURT: Why would the business have earnings?

4 MR. SERINO: It has no --

5 THE COURT: Then you'd only have a one million dollar
6 depreciation deduction and you'd have another eighteen million
7 dollars in income.

8 MR. SERINO: Fair enough. I was saying that if he
9 wants to stay with his forty million dollar depreciation and he
10 wants to pay all his capital expenditures with that
11 depreciation, he's going to wipe out his adjusted after-tax
12 cash flow.

13 THE COURT: Okay.

14 MR. SERINO: Gone. Zero.

15 MR. PARKINS: Can I respond to that point, Judge?

16 THE COURT: Is there anybody else --

17 MR. PARKINS: Yeah, the answer is, Your Honor --

18 MR. SERINO: And --

19 MR. PARKINS: -- it's very simple. I'm sorry.

20 THE COURT: Oh, I sort of -- okay.

21 MR. PARKINS: No, I'm sorry. I just want to check
22 something.

23 THE COURT: I think we can wrap this up pretty soon.

24 MR. PARKINS: Yup.

25 MR. SERINO: I guess the only point I wanted to make,

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1 Your Honor, was the opening statements that counsel referred
2 to -- I talked about you don't look at what the buyer's going
3 to do with the business. If you read the rest of that
4 sentence, what I meant is you don't look at improvements that
5 the buyer's going to make to the business. And that's what
6 Rash says. You don't look at the -- the creditor doesn't get
7 the benefit of modifications to the equipment. If the creditor
8 has --

9 THE COURT: Modifications that aren't subject --

10 MR. SERINO: To his lien.

11 THE COURT: -- to his lien.

12 MR. SERINO: Right.

13 THE COURT: But somebody's going to spend more for it
14 because they can modify it to be more productive. Why can't
15 you consider that?

16 MR. SERINO: Because the firsts don't have a lien on
17 that. And Rash says you got to value the car, and if you put a
18 lien on the car and then thereafter the car's modified with a
19 new sound system, a radar, a new engine, the first doesn't have
20 a lien on all of those elements.

21 THE COURT: Okay. Mr. Serino, I just think we're
22 talking at cross purposes.

23 MR. PARKINS: Your Honor, I just have thirty seconds.

24 THE COURT: Thirty seconds. I'm timing you.

25 MR. PARKINS: Your Honor, if taking Mr. Serino's

1 example of increasing the capital expenditures and would wipe
2 out the depreciation, that's nonsense because you increase
3 capital expenditures to drive more money. You spend more money
4 to get more money.

5 THE COURT: Yeah, but you can't depreciate your
6 property beyond what you spend for it. And you can't spend --

7 MR. PARKINS: No, but if you spend more money for
8 capital expenditures, you would always have more value to
9 depreciate going forward. His scenario was if you brought
10 capital expenditures up, you'd wipe out the cash flow. No.
11 You bring capital expenditures up is to drive more cash flow
12 because you're enhancing the business.

13 THE COURT: All he's saying is you cannot spend a
14 million dollars on equipment and depreciate nineteen million
15 dollars forever. The numbers don't --

16 MR. PARKINS: That is true.

17 THE COURT: We're agreed on that.

18 MR. PARKINS: Thank you, Your Honor.

19 THE COURT: Give you the last word.

20 MR. QURESHI: Thank you, Your Honor. I've got three
21 points, and I promise they are very quick.

22 THE COURT: All right. I'm counting.

23 MR. QURESHI: First point: going-concern value.
24 Confusion about going-concern value versus premises value as a
25 going concern, what Mr. Beaton did.

1 THE COURT: I didn't think it was confusing until I
2 listened to Mr. Serino.

3 MR. QURESHI: Your Honor, the statement by counsel
4 for the first liens that to the extent that the Lazard number
5 is sixty million dollars higher on a going-concern basis, that
6 that's their value, no, it's not. That's going-concern value.
7 That's what we're talking about. It isn't intangible. We have
8 case after case after case in our pleading that says that
9 going-concern value isn't intangible assets.

10 Now, Your Honor's specific back-and-forth with Mr. --

11 THE COURT: Okay. So if you assume that the number
12 is 273, and I think that Mr. Schmitt used the same method for
13 determining enterprise valuation that business value is
14 generally used, we're putting the name replacement value on it
15 but that's what he did. And if you came up with 337 and you
16 backed out the 174 for working capital and the 28 for
17 intangibles, what's left is the PP&E, right?

18 MR. QURESHI: Well, Your Honor, I think that's coming
19 at it from the wrong direction. You have to start at the
20 bottom of this.

21 THE COURT: That's a different valuation. What
22 you're telling me is you cannot accept a top-down valuation --

23 MR. QURESHI: What I'm telling you --

24 THE COURT: -- either the debtor's or Lazard's or Mr.
25 Lerman's. That's what you're saying.

16 My second point, Your Honor, deals with the
17 suggestion that what Mr. Beaton did here was value a catalog of
18 used parts. That would be a liquidation. Again, Mr. Beaton
19 assumed an assemblage of assets staying in place where it is
20 today being operated in the business it is today. That is a
21 textbook definition of a going concern in terms of value.
22 Liquidation assumes the assets are not going to stay in place,
23 they're not going to stay together and there will be value
24 piece by piece, broken down, some just for scrap value. That's
25 not what he did.

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5 THE COURT: Thank you. Come back at 3:30. I'll
6 rule.

7 (Recess from 2:23 to 4:08 p.m.)

21 Wellman is engaged in the business of producing
22 polymers and fibers. It operates the Pearl River plant in Bay
23 St. Louis, Mississippi, the Palmetto plant in Darlington, South
24 Carolina and the Johnsonville plant in Johnsonville, South
25 Carolina.

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1 Wellman produced polyethylene terephthalate, or PET,
2 resin at Pearl River and Palmetto. It also produces polyester
3 staple fiber at Palmetto. According to the draft disclosure
4 statement received in evidence as BNY Exhibit 1, the products
5 produced at Palmetto and Pearl River comprise Wellman's
6 chemical segment and account for approximately ninety-five
7 percent of its overall sales.

8 Finally, Wellman produced nylon engineering resin at
9 the Johnsonville plant.

10 The real estate and other physical property located
11 at the three plants comprise Wellman's PP&E. Wellman also owns
12 some physical property located at a corporate headquarters, but
13 none of the experts ascribed any material value to these
14 assets.

15 Wellman owes approximately 185 million dollars to
16 BNY. BNY is secured by a first lien on the PP&E. BNY does not
17 have a lien in Wellman's other assets, including its working
18 capital and general intangibles.

19 Wellman has proposed a plan under which it will
20 obtain the PP&E and use it in connection with its post-
21 confirmation operations. Anticipating that BNI will reject the
22 plan and Wellman will need to cram it down, Wellman has moved,
23 pursuant to Federal Bankruptcy Rule 3012, to value BNY's
24 collateral.

25 As noted, the Court conducted a two-day hearing.

1 Wellman's expert, Richard Schmitt of AccuVal Associates,
2 testified that the PP&E had a replacement value of
3 approximately 70.8 million dollars. BNY's expert, David Lerman
4 of Huron Consulting Group, opined that the replacement value
5 ranged between 136.8 million and 189.4 million, depending on
6 what intellectual property and other intangibles were included
7 in computing the value.

8 Finally, Neil Beaton of Grant Thornton LLP was
9 retained by Wilmington Trust Company, a second lien term loan
10 agent ("Wilmington"). He stated that the replacement value of
11 the PP&E was 74.3 million.

12 The Court received other possible indications of
13 value during the hearing. Wellman had attempted to sell its
14 assets both before and after the petition date. Toward that
15 end, it retained Lazard Freres & Co. to manage the sale
16 process.

17 According to Andrew Yearley of Lazard, the highest
18 and best offer that Wellman received was 260 million for all of
19 its assets.

20 In addition, Keith Phillips, Wellman's CFO, testified
21 that Wellman took an "impairment loss" in March 2008 pursuant
22 to FAS 144. As a result, Wellman wrote down the value of its
23 net PP&E from approximately 525 million dollars to 242 million
24 dollars.

25 Lastly, Wellman's disclosure statement described a

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1 total enterprise value between 298 million and 373 million and
2 valued the PP&E, for liquidation purposes, at 65.8 million
3 dollars, exclusive of the cost of liquidation.

4 The Court has jurisdiction over this proceeding
5 pursuant to 28 U.S.C. Sections 1334(b) and 157(a) and the
6 standing order of reference signed July 10, 1984. Venue was
7 proper under 28 U.S.C. Section 1409(a). This is a court
8 proceeding pursuant to 28 U.S.C. Section 157(b)(K), (L) and
9 (O).

10 Section 1129(b)(2) of the Bankruptcy Code permits a
11 plan proponent to cram a plan down over a rejection by a class
12 of secured claims. Where the debtor proposes to retain the
13 collateral for post-confirmation operations, the debtor can
14 cram down the plan by paying the secured creditor the allowed
15 amount of the secured claim as of the effective date.

16 This means that if the debtor pays over time, it must
17 also pay interest. If the secured creditor makes the Section
18 1111(b) election, the aggregate amount of the payments must
19 equal the full amount of the total claim, both secured and
20 undersecured.

21 In either case, it is necessary to determine the
22 allowed amount of the secured claim as of the effective date,
23 which the parties have assumed to be September 30, 2008.

24 Under Section 506(a), the amount of the secured claim
25 depends on the value of the creditor's interest in the debtor's

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1 interest in the property that secures the claim, that is, by
2 the value of the collateral.

3 Furthermore, the Court must determine the value in
4 light of the purpose of the valuation and the proposed
5 disposition or use of the collateral.

6 Where the debtor proposes to retain the collateral
7 for use in its post-confirmation operations, the appropriate
8 measure is the collateral's "replacement value". See
9 *Associated Commercial Corp. v. Rash*, 520 U.S. 953, 960 (1997).
10 The replacement value is "the price a willing buyer in the
11 debtor's trade, business or situation would pay to obtain like
12 property from a willing seller," *id.*, and corresponds to the
13 "fair market value." See *id.*, at 959, note 2. This involves a
14 valuation on a going concern rather than a liquidation basis.
15 All parties agree that this is the appropriate standard, and it
16 is the standard that the experts attempted to apply.

17 The evidence showed that valuation is not a science
18 but an art, and a very subjective one at that. While the
19 experts in this case testified honestly and candidly, their
20 conclusions were greatly affected by the assumptions that they
21 made.

22 The evidence revealed two general approaches to the
23 valuation of the PP&E. Under the top-down approach, the entire
24 enterprise's value, using one or more of the generally accepted
25 techniques, primarily the income and market approaches,

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1 Wellman's counsel contended, at closing argument, that
2 Schmitt's top-down methodology somehow differed from Lazard's
3 and implied that they were measuring different enterprise
4 values. Yet, the Schmitt report and the disclosure statement
5 described the respective methodologies for determining
6 enterprise value in substantially the same manner.

7 The enterprise value consists of three elements: the
8 PP&E, or the physical assets; the working capital, or financial
9 assets; and the intangibles. The intangibles include the
10 customer and supplier relationships, the workforce, the patents
11 and trademarks and the intellectual property.

12 Under the top-down approach, the appraiser must
13 compute the value for the entire enterprise and then value and
14 back out the working capital and intangibles which do not
15 collateralize BNY's debt.

16 This approach has obvious drawbacks. It requires the
17 expert to value all of the assets when the focus is the PP&E.
18 As a result, it multiples the analysis and a host of
19 assumptions regarding value. These can lead to wildly
20 disparate results, as made evident by the comparison of the
21 reports and testimony provided by Wellman's and BNY's experts
22 and Lazard's conclusions in the disclosure statement.

23 Wellman's experts fixed the enterprise value at 273
24 million dollars. Using similar methodology, BNY estimated an
25 enterprise value of 366 million, under one of its scenarios, or

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1 113 million more than Wellman. Lazard found a range of values
2 with a midpoint of 337 million.

3 The second approach values the PP&E from the bottom
4 up. Using the company's books and records, the appraiser first
5 determines the original cost of the PP&E. Here, Wellman
6 maintained accurate historical cost records for all of its
7 physical assets. The appraiser must then make a series of
8 adjustments that take into account the physical condition of
9 the equipment and external factors and other costs in delay.
10 Under this approach, it is unnecessary to value the enterprise
11 or the working capital or the intangibles.

12 After considering the testimony and the reports of
13 the experts, I conclude that the bottom-up cost approach is the
14 more reliable indicator of the value of the PP&E, at least up
15 to a point.

16 As noted, Wellman and BNY offered wildly divergent
17 results, and their experts' analyses often strain credibility.
18 For example, Lerman responded to several questions during
19 cross-examination to the effect that he did not have all the
20 information he needed to conduct his valuations because Wellman
21 refused to provide it. Although I don't blame Lerman for this
22 shortcoming, the lack of necessary information undercuts the
23 probative value of his opinion.

24 More specifically, Lerman's discounted cash flow
25 analysis assumed depreciation into perpetuity that vastly

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1 exceeded the project capital expenditures. At this rate,
2 Wellman would exhaust its depreciation deduction in a few years
3 well short of perpetuity.

4 In addition, he assumed the same thirty-five year
5 useful life for the equipment at Pearl River and Palmetto, even
6 though the equipment at one of the plants was only nine years
7 old and the equipment at the other was as much as thirty-five
8 years old.

9 Finally, Lerman assumed that the price of natural
10 gas, an important component of Wellman's costs, would not
11 increase. The evidence at trial showed that it had already
12 increased substantially.

13 Schmitt's opinion also raised some credibility
14 concerns. He consistently picked low ratios, such as under the
15 Guideline Public Company Method, which had the effect of
16 depressing Wellman's enterprise value.

17 Furthermore, while Lerman was criticized for failing
18 to properly compute the terminal value under his discounted
19 cash flow analysis, Schmitt did the same thing.

20 Moreover, Schmitt's enterprise value came in far
21 below Lazard's, who was not valuing Wellman for litigation
22 purposes.

23 In contrast to the top-down approach, the bottom-up
24 approach is more straightforward. It requires fewer subjective
25 judgments and assumptions compared to the top-down approach.

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1 Beaton applied this approach exclusively. Wellman's
2 expert also applied a bottom-up methodology, among several, but
3 his testimony was less credible. His conclusion regarding
4 value turned on a substantial reduction attributable to an
5 economic penalty in the aggregate amount of more than 128
6 million dollars. Neither his testimony nor his report
7 adequately explained a deduction of this magnitude, and it
8 appears to have been selected to make the top-down and bottom-
9 up valuations match exactly.

10 Beaton's testimony and report were far more precise
11 and helpful in terms of explaining the methodology and the
12 conclusions and, accordingly, I rely on it for the balance of
13 this decision.

14 As noted, Beaton began by first determining Wellman's
15 historical cost for its PP&E. He then determined what it would
16 cost to buy the same equipment new by using generally accepted
17 price indices to take into account changes in costs.

18 Since the PP&E is not new, Beaton then had to reduce
19 the PP&E to its depreciated replacement cost. He did this by
20 making deductions for functional and economic obsolescence.
21 Functional obsolescence refers to the loss of value or
22 usefulness caused by the inefficiencies or inadequacies of the
23 property itself and also takes into account the development and
24 deployment of more efficient and less costly replacement
25 property.

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1 Economic obsolescence refers to the loss of value
2 external to the property and may include the economics of the
3 industry, the availability and/or increased costs of financing,
4 labor and raw materials, legislation, reduced demand, increased
5 competition and similar factors.

6 In the case of the machinery and equipment, Beaton
7 used valuation software to determine the offsets resulting from
8 general functional and economic obsolescence. He used
9 comparable sales to determine the current value of Wellman's
10 real estate and then made further obsolescence deductions.

11 Beaton concluded that the aggregated depreciated
12 replacement cost for all of Wellman's PP&E was approximately
13 296 million dollars. No one has mounted a serious challenge to
14 his computations to this point, and it represents the ceiling
15 of replacement value.

16 None of the parties, however, contend that a willing
17 buyer would spend this much for Wellman's PP&E. With all of
18 the analysis that has already accounted for the physical
19 condition of the equipment and certain general obsolescence,
20 the value of the PP&E at bottom is determined by its ability to
21 generate income to the hypothetical buyer and the time and
22 effort it will take to do so.

23 Like book value, the depreciated replacement cost
24 does not necessarily reflect the fair market value or
25 replacement value of the asset. Hence, it is necessary to

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1 reduce the depreciated replacement cost to reflect what Beaton
2 termed physical and economic obsolescence specific to Wellman's
3 PP&E.

4 This is the point at which Beaton's analysis became
5 highly speculative. Beaton reduced the depreciated replacement
6 cost by an aggregate of seventy-five percent through two
7 additional deductions. First, he reduced it by fifty percent
8 to account for what he termed specific economic obsolescence.
9 According to Beaton, specific economic obsolescence referred to
10 the historical inability of the PP&E to generate positive cash
11 flow to Wellman's financial condition, globalization,
12 oversupply and high raw material costs. It also included the
13 relocation cost that the hypothetical buyer would have to
14 incur.

15 Second, he reduced that result by another fifty
16 percent based on selling and holding costs. These consisted of
17 the delay that the hypothetical buyer would face in introducing
18 the intangible assets, customer and supplier relationships,
19 intellectual property to assemble a work force that give the
20 PP&E its value.

21 The selling and holding costs also included the cost
22 of achieving a state of installation, such as construction,
23 installation, engineering, financing and start-up costs.

24 As Beaton himself conceded, the two, fifty percent
25 deductions were unscientific and subjective, although I suspect

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1 that BNY might call them arbitrary.

2 Based on these assumptions and the corresponding
3 deductions, Beaton opined that the replacement value of the
4 PP&E equaled 74.3 million dollars, or 25 percent of the
5 depreciated replacement cost.

6 I reject this conclusion because the admittedly
7 subjective fifty percent reductions suffered from some obvious
8 flaws. First, the specific economic obsolescence was based on
9 Wellman's historical inability to generate positive cash flow
10 with the PP&E. The evidence indicated that there were numerous
11 competitors in the industry that operated at substantially
12 higher profit margins than Wellman. For example, Wellman's
13 gross operating profit margin in 2007 was 5.4 percent.
14 According to Exhibit 7 in the Huron report at page 91,
15 Wellman's competitors had an average gross operating profit
16 margin of 16.8 percent in 2007. In other words, the
17 hypothetical buyer in Wellman's industry generates more profit
18 with comparable assets.

19 Second, there was an overlap between the general
20 economic obsolescence considered in reaching the depreciated
21 replacement cost and the specific economic obsolescence that
22 Beaton applied after he computed the depreciated replacement
23 cost.

24 For example, both the general and specific
25 obsolescence included considerations of competition, supply and

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1 demand and the cost of raw materials. Although Wellman
2 attempted to distinguish between the general and specific
3 factors of competition, supply and demand and raw materials, I
4 cannot discern the difference from this record. Hence, there
5 appear to be some double-counting.

6 Third, many of the factors that Beaton identified
7 under the rubric of selling and holding costs correspond to the
8 definition of intangibles. Beaton assumed that the delay in
9 reintroducing customer and supplier relationships, workforce,
10 IP and the like would severely impact the replacement value.
11 The selling and holding deduction accounted for a 74 million
12 dollar drop in replacement value, although if Beaton had
13 applied this 50 percent deduction first instead of second, it
14 would have resulted in a 148 million dollar decline.

15 In any event, this is just another way of saying that
16 the intangibles in place make up as much as fifty percent of
17 the replacement value of the PP&E. Neither of the other
18 experts ascribe this magnitude of value to Wellman's
19 intangibles.

20 Moreover, the hypothetical buyer is already operating
21 in Wellman's industry and would bring some of these same
22 intangibles to the table.

23 Furthermore, Beaton's direct approach was supposed to
24 avoid the need to compute and back out the value of the other
25 components of enterprise value. Yet this is precisely what he

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1 did indirectly with the intangibles.

2 Fourth, although I would not characterize it as
3 double-dipping, there was some overlap between the specific
4 economic obsolescence and the selling and holding factors. At
5 his deposition, Beaton identified many of the same factors as
6 comprising economic obsolescence, on the one hand, and selling
7 and holding costs, on the other.

8 Although he attempted to draw a sharper distinction
9 at trial, both deductions still included, to varying degrees,
10 the cost of installing the PP&E at the new location and getting
11 it up and running.

12 Fifth, Beaton assumed that it would take a
13 hypothetical buyer three to six months to get the new PP&E up
14 and running. The Pearl River plant was destroyed by Hurricane
15 Katrina in 2005 but was back up and running in sixty days.
16 Thus, the three to six-month delay during which the assets
17 would not generate any income appears to be overly
18 conservative.

19 Sixth, Beaton's and Schmitt's going-concern
20 valuations were nearly equal to the liquidation value that
21 Wellman ascribed to the PP&E. According to Wellman's proposed
22 disclosure statement, the PP&E would be worth approximately
23 sixty-six million at liquidation, exclusive of liquidation
24 expense. This was approximately 5 million dollars less than
25 Schmitt's valuation and 8.5 million dollars less than Beaton's

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1 valuation. It also reflected twenty-seven percent of the book
2 value, the same approximate ratio that existed between Beaton's
3 depreciated replacement costs and the replacement value.

4 The going-concern value is presumably greater than
5 the liquidation value. Cf. *In re: BFP*, 511 U.S. 531 at 538-39
6 (1994) (stating that the "fair market value" was the
7 "antithesis" of the forced-sale value). If it were not, it
8 would mean that the PP&E is incapable of generating cash flow
9 beyond its scrap value. The proponents of the lower valuations
10 have not offered a cogent explanation of how the liquidation
11 and going-concern values for income-producing PP&E can be
12 virtually the same.

13 In short, I conclude that the evidence does not
14 support the magnitude of deductions that Beaton took for the
15 specific economic obsolescence and selling and holding costs.
16 Accordingly, I reject these deductions that aggregate seventy-
17 five percent of the depreciated replacement cost. Instead, I
18 find that these deductions should be limited to a single fifty
19 percent deduction with some further modification.

20 Applying the single fifty percent reduction, the
21 replacement value of the PP&E would be 148 million. This sum
22 will be reduced to 140 million, which is consistent with the
23 result that would be reached if Lazard's midpoint enterprise
24 value is substituted for Schmitt's.

25 Finally, I do not find that Phillips' or Yearley's

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1 testimony assists in determining the replacement value of the
2 PP&E. The asset impairment reduction reflected accounting
3 considerations. The relationship between the reduced book
4 value of the PP&E, for accounting purposes, and the replacement
5 value that a hypothetical buyer would pay for the PP&E has not
6 been demonstrated.

7 Yearley's testimony regarding Wellman's sales efforts
8 indicated that Wellman was under severe financial and time
9 pressures to sell. Although Yearley testified that the
10 relatively accelerated selling effort did not affect the price,
11 the evidence showed that the "expressions of interest" dropped
12 substantially after the petition date when the Court entered a
13 DIP financing order containing a drop-dead sale date.

14 Wellman was under a compulsion to find a buyer. It
15 wasn't merely a willing seller; it was an overanxious one. For
16 this reason, the bids that Wellman obtained should not be
17 considered an accurate measure of the PP&E's replacement value,
18 as that term is defined in Rash.

19 In summary, I conclude that the replacement value of
20 the PP&E is 140 million dollars. The foregoing constitutes the
21 Court's findings of fact and conclusions of law. Settle an
22 order on notice.

23 MR. SPEAKER: Thank you.

24 THE COURT: Thank you for a well-tried case.

25 ALL: Thank you, Your Honor.

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1 THE COURT: Good luck.

2 (Whereupon these proceedings were concluded at 4:33 p.m.)

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2 I N D E X

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4 R U L I N G S

5 DESCRIPTION PAGE LINE

6 Court finds replacement value of the debtors'
7 PP&E is 140 million dollars and directs counsel
8 to settle an order on notice

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2 C E R T I F I C A T I O N

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4 I, Lisa Bar-Leib, certify that the foregoing transcript is a
5 true and accurate record of the proceedings.

6 **Lisa Bar-Leib**

Digitally signed by Lisa Bar-Leib
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8 **LISA BAR-LEIB**

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15 **Date: August 6, 2008**

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